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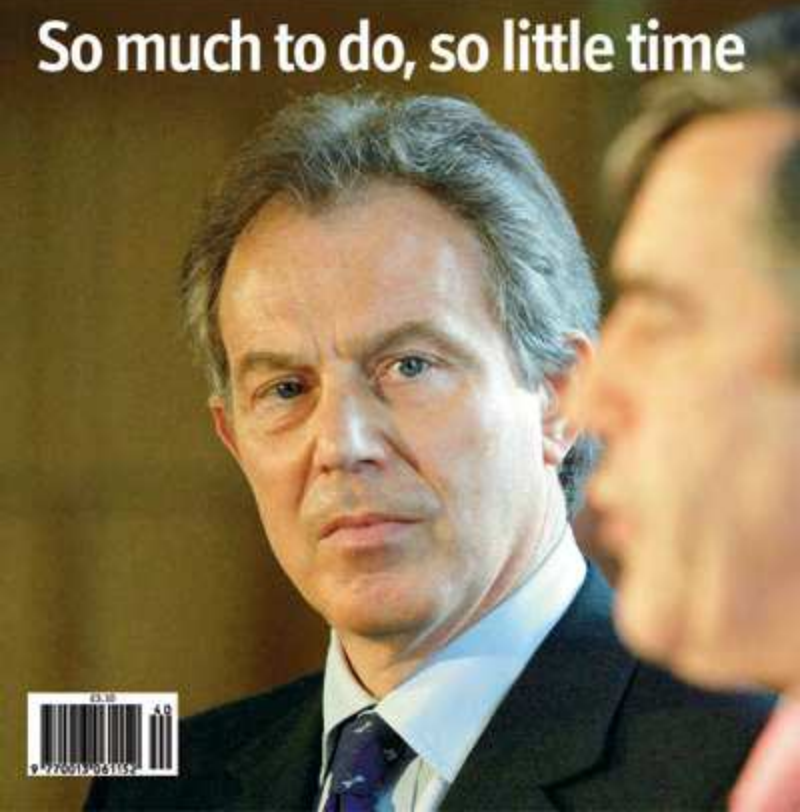

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Politics this week

Sep 29th 2005
From The Economist print edition

A Hammer blow

Tom DeLay, the majority leader in the House of Representatives, was indicted by a grand jury in a long-running investigation into campaign-finance donations in Texas. Mr DeLay, considered one of Washington's less genteel political operators, stepped down, at least temporarily, from his position and accused his prosecutors of being politically motivated. Separately, **Bill Frist**, the Senate's majority leader, said he would co-operate with federal authorities investigating the possible insider trading of shares in HCA, a hospital business founded by his family. See article

George Bush visited Louisiana and Texas to survey the damage wrought by **Hurricane Rita**. Meanwhile, Michael Brown, who resigned as head of the Federal Emergency Management Agency over its response to Hurricane Katrina, told a Senate committee that a lack of co-ordination between Louisiana's state and local agencies was to blame for the poor relief effort there. See article

An estimated 100,000 protesters held a series of **demonstrations against the Iraq war** in Washington, DC, the largest such protest in America since the invasion in March 2003. Dozens of people, including Cindy Sheehan, a mother who camped outside George Bush's Texan ranch, were arrested after staging a sit-in near the White House. See article

EPA

Lynndie England, the soldier who was famously photographed leading a naked Iraqi prisoner on a leash at the **Abu Ghraib** prison, was sentenced to three years in jail.

A violent turn

A suicide-bomber killed at least 12 people outside an army base in Kabul. Such attacks have been rare in **Afghanistan**, despite an upsurge in violence by Taliban insurgents this year.

Indonesia deployed thousands of extra police in Jakarta and other cities ahead of an increase in fuel prices that was expected to spark protests. See article

Two more people died from **bird flu** in Indonesia, taking the death toll in the country's current epidemic to five.

Pakistan said it had arrested a Sunni militant, Asif Chotu, who is wanted in connection with dozens of attacks against the Shia minority. Sectarian violence has killed thousands in the past 25 years.

Looking up for Lula

In a boost for **Brazil's** embattled president, Luiz Inácio Lula da Silva, his government's candidate won an election for the presidency of the lower house of Congress. The government has been rocked by allegations of corruption and illegal party financing.

In **Venezuela**, the father of President Hugo Chávez, who is a state governor, issued a decree expropriating a flour mill belonging to Polar, the country's largest private firm. Officials have recently taken over dozens of farms.

Canada's finance minister, Ralph Goodale, said he would not issue promised guidelines for bank mergers before an election due next year. He also backed away from a previous promise to reintroduce corporate tax cuts that were withdrawn from this year's budget in return for the leftish New Democrats supporting the Liberal minority government.

A judge in the United States has ruled that Luis Posada Carriles, wanted for allegedly blowing up a Cuban airliner in 1976, killing 73 people, cannot be deported to either **Cuba** or Venezuela.

In **Peru**, the trial began of Abimael Guzmán, the founder of Shining Path, and 23 other leaders of the Maoist guerrilla movement which terrorised the country in 1980-93. Mr Guzmán was sentenced to life imprisonment by a military court in 1993. But ten years later the constitutional tribunal ordered a retrial by a civilian court.

Reuters

On a visit to **Haiti**, Condoleezza Rice, America's secretary of state, told the interim government to speed up the arrangements for an election fixed for November 20th. During her visit, gunmen raided an election office, carrying off its computer.

The bulldozer gets through

A split in **Israel's** ruling Likud party was deferred after its central committee voted narrowly not to bring forward the leadership primaries that will pit Ariel Sharon, the prime minister, against his main rival, Binyamin Netanyahu. See article

After the heaviest fighting between militant **Palestinians** and the Israeli army this year (particularly in the Gaza strip), a threatened return to full-scale violence was averted when both Hamas and Islamic Jihad said they would return to a ceasefire brokered in March.

The American army in **Iraq** said it had killed Abdullah al-Juwairi, better known as Abu Azzam, second in rank to Abu Musab al-Zarqawi, al-Qaeda's proclaimed leader in the country. But suicide-bombings continued unabated.

Iran threatened to use trade and oil contracts to punish the 22 countries on the board of the International Atomic Energy Agency that had voted to report it (though with no deadline) to the UN Security Council for violating its non-nuclear obligations. These included India and Japan, both with big energy interests in Iran. Russia and China were among 12 abstentions.

South Africa's annual report on crime statistics showed a drop in most categories of crime, including murder and burglary. See article

The wages of terrorism

A court in **Spain** sentenced Imad Yarkas, a Syrian who is also known as Abu Dahdah, to 27 years in prison for aiding the September 11th 2001 attacks in America. Another 17 men were convicted of helping al-Qaeda. However, prosecutors had pressed for a murder charge to be brought against Mr Yarkas (and two others) and sought sentences of 74,000 years on behalf of the victims of the attacks.

Poland's centre-right won the country's general election, ousting the governing Democratic Left Alliance from power. The Law and Justice Party, which with 27% gained the largest share of the vote, nominated Kazimierz Marcinkiewicz, an economist, as prime minister. After four years of ex-communist government, Poland's unemployment rate of 18% is the highest in the European Union. See article

EPA

The independent commission monitoring the disarming of the **Irish Republican Army** in Northern Ireland said that its weapons had "been put beyond use", and indicated the process was complete. Some Unionists complained of insufficient evidence. See article

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Business this week

Sep 29th 2005
From The Economist print edition

Oil's well that ends well

In Russia's biggest-ever takeover, **Gazprom**, the country's gas monopoly, agreed to buy a 72.7% stake in **Sibneft**, an oil firm, for $13.1 billion (its total stake now stands at 75.7%). Gazprom made the deal with Millhouse Capital, Roman Abramovich's investment firm. It marks the last divestment of a major Russian business by Mr Abramovich, who is based in London but is one of Russia's wealthiest business "oligarchs". See article

In another big merger among America's health insurers, **WellPoint** announced a $6.5 billion takeover of **WellChoice**, a smaller rival based in the New York metropolitan area. Analysts have been expecting WellPoint, the country's largest health insurer, to make a large acquisition following UnitedHealth Group's purchase of Pacificare Health Systems in July.

UBS said it was negotiating a SFr272m ($210m) stake in **Beijing Securities**, a mid-sized brokerage that operates across China. Earlier, the Swiss financial group announced that it will also take a 1.6% stake in **Bank of China** for SFr645m —BoC's third investment deal with foreign institutions since mid-August.

Equitable Life came under pressure from policyholders to explain last week's decision to drop a negligence claim against Ernst & Young, the firm's former auditor which it blames for its near-collapse in 2000. The litigation has cost Britain's oldest mutual insurer at least £30m ($54m). Equitable was also reportedly close to cutting a deal with 15 former directors with whom it is in dispute. See article

In the driver's seat

Porsche wants to increase its stake in **Volkswagen** to 20%. The German luxury carmaker hopes to shield VW, which supplies it with components, from hostile takeovers. But the deal, worth around *euro*3 billion ($3.6 billion), was viewed with scepticism by some who questioned Porsche's wisdom in tying its fortunes closer to VW's. Porsche's share price fell by 10% after the announcement, although it later rallied. See article

DaimlerChrysler outlined a plan to offer redundancy to 8,500 workers at its **Mercedes** division in Germany. The carmaker said the move would cost *euro*950m ($1.1 billion), which it would recoup in efficiency and savings gains.

Union leaders at **Boeing** recommended that its members return to work after the terms of a new contract were agreed on. Around 19,000 machinists and auxiliary staff have been striking over proposed changes to benefits, but Boeing now says it will boost pensions and not increase the costs of health insurance.

US Airways officially completed its merger with **America West Airlines** and began trading as a

single company after a year of restructuring so it could emerge from bankruptcy. Coming soon after Delta and Northwest sought bankruptcy protection and amid high fuel-costs, the event provided welcome news for America's carriers.

The Stringer show

Investors took a dim view of **Sony's** revival plan, unveiled last week. The company's share price in Tokyo fell, wiping out recent gains. Moody's said it was reviewing Sony's credit rating over concern that the potential for low profits in its electronics unit would stymie the proposed turnaround. See article

Sony also suffered a blow in its prominent backing of the much-touted Blu-ray technology for the next generation of **high-resolution DVDs.** Both Intel and Microsoft backed Toshiba's rival HD-DVD format as the industry standard.

Britain's economy has been weaker than statisticians previously thought. Revised figures indicated that GDP grew by 1.5% in the year to the second quarter, the slowest pace for 12 years. See article

Lester Crawford resigned as head of America's **Food and Drug Administration**, less than three months after he was confirmed in the job. The FDA has come under intense criticism recently for approving the sale of Vioxx, and faces a potential political storm over a delayed decision on access to morning-after contraceptives. See article

Oil prices traded at around $65 per barrel as oil companies in Texas said that Hurricane Rita had a limited effect on their refining capacity. Separate reports indicated that widespread damage to oil rigs in the Gulf coast could affect production. Meanwhile, George Bush urged Americans to cut back on the use of their cars in an effort to save petrol. See article

Capricious Katrina

The Conference Board reported its index of American **consumer confidence** had dropped by 19 points in September, the biggest fall in 15 years. Hurricane Katrina and high petrol prices were blamed, but analysts suggested a weakening housing market and inflationary fears may also affect consumers' long-term confidence.

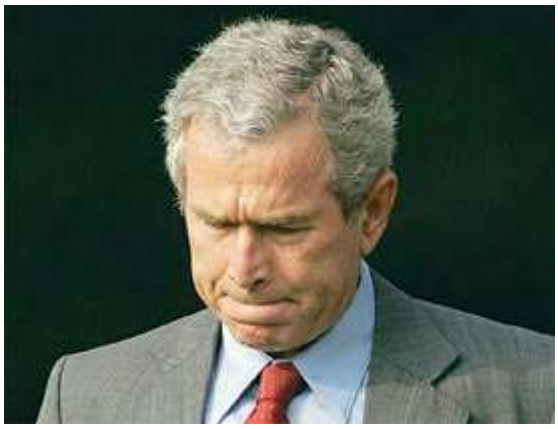
The Republican crisis

What's gone wrong for America's right

Sep 29th 2005
From The Economist print edition

George Bush's Republicans are in trouble, but if he has the will and the wit he can fix their problems

AP



Get article background

FOR George Bush September has been the cruellest month. The news from Iraq continues to be grim. Hurricane Katrina—and his initial cluelessness in dealing with it—sent his approval ratings to new lows. Mercifully, Rita was less ferocious. But in the meantime the conservative coalition that he heads and which dominates American politics has become engulfed in a political storm of its own.

In Katrina's wake, rows have broken out about the very unconservative increase in public spending and the cronyism of Mr Bush's appointments. Meanwhile, a party which came to power by running against the sleaziness of Washington, DC, has got engulfed in corruption scandals of its own. First the White House's top procurement official was indicted. Then the Securities & Exchange Commission announced an investigation into share dealing by Bill Frist, the Senate majority leader. Now—and most seriously—the House majority leader, Tom DeLay, has been indicted in a Texan corruption probe. The Hammer has been forced to step down “temporarily”.

It is easy to exaggerate the nature of the “conservative crack-up”. Some of the blame for post-Katrina incompetence belongs to local Democrat officials in Louisiana, and Mr Bush did a better job of handling Rita. Mr DeLay says the investigation into his affairs (run by pretty much the last Democrat in Texas) is politically motivated. Mr Frist seems to have an innocent explanation for his share sale. Bits of the conservative machine continue to grind forward: as *The Economist* went to press, it looked likely that John Roberts would be confirmed as chief justice of the United States. It would be foolish to bet on the chaotic Democrats winning back Congress next year: in the Senate, they are defending more seats, and in the House, gerrymandering makes most incumbents very difficult to shift.

Yet there is plainly more going on than just one bad month. Mr Bush's domestic programme—notably his plan to overhaul Social Security—lies in tatters; and his attention must have drifted from matters overseas. More importantly, the current crisis points to deeper difficulties, to do with competence, cronyism and the contradictory nature of “big government conservatism”. It is not too late for Mr Bush to deal with these things; but he must do so brutally and quickly—and not just for his party's sake. It is not in anybody's interest—even those now smug Europeans who loathe Mr Bush's America—for Mr Bush to become a lame-duck president consumed by domestic woe.

The Economist has always had all sorts of ideological disagreements with Mr Bush, but our main problem with his administration has increasingly become incompetence. Katrina now stands besides the shambles overseas in Iraq and Guantánamo Bay as supporting evidence. Mr Bush is a bold decision-maker, but he is also a delegator who too often picks the wrong people and seldom fires them. Both “Rummy” and “Brownie” (ie, Donald Rumsfeld, the defence secretary, and Michael Brown, the erstwhile Arabian-horse man whom Mr Bush belatedly removed from the Federal Emergency Management Agency) are symptoms of the same problem.

America's system of political appointees always risks putting the well connected, rather than the well qualified, into top jobs. But Mr Bush has abused this more than most. One advantage of Republicans is they normally want to restrict government. Yet Mr Bush and Mr DeLay have embraced big-government conservatism. Like Lyndon Johnson's Democrats in the 1960s, they believe they can use the state to do good—but this time for conservative, not liberal, ends. This is not quite as oxymoronic as it first sounds: you can indeed use government cash to make schools more accountable and promote families. But it has come with two serious flaws.

The most important is fiscal profligacy. Mr Bush has increased spending more than any president since Johnson, and cut taxes with the enthusiasm of Ronald Reagan. Second, far too much cash has gone on earmarked pork-barrel projects without economic justification. There is $24 billion-worth of such gunk in the highway bill, including the notorious $231m “bridge to nowhere” in Alaska, put there by the chairman of the House transportation committee. When Mr DeLay, the man who led the Republican takeover of K Street, the lobbyists' home in Washington, DC, announced a couple of weeks ago that the budget was “pared down pretty good”, it is hardly surprising that the anti-tax wing of his party went mad.

Katrina the cleaner and Teddy Roosevelt

What does Mr Bush need to do? One priority is a proper audit of what went wrong with Katrina. This week, “Brownie” was hauled in front of Congress and harangued for his incompetence. This should remind other cronies of the administration that plum federal postings carry responsibilities, but Mr Brown was right to protest that he was not to blame for everything. Mr Bush is currently resisting attempts to set up an independent inquiry into what went wrong: he would prefer to have an inquiry led by a White House adviser. This is heinous. A thousand people have died and the tax payer faces a bill of up to $200 billion. If those two things do not merit independent investigation, then what on earth does?

The second priority is to tackle profligacy and pork. A good symbolic first step would be for Mr Bush to back a “pork-for-reconstruction” scheme, where politicians give up projects earmarked for their districts, so the proceeds can go to New Orleans; better still he should urge them to get rid of earmarking completely. More important, he should look at the contradictions underlying his brand of conservatism. That means promoting serious spending cuts, especially in entitlement programmes, and giving up some of his cherished tax cuts.

Every successful political movement has its contradictions. It is much harder to survive them if

you are inefficient and stained by corruption. It is hard to imagine that Mr Bush—a conviction politician if ever there was one—wants to be remembered for the messy bungling of this cruel September. He might take a look at Teddy Roosevelt, the first big-government conservative; he was also famous for waging war against corruption and cronyism. Now is a good time for Mr Bush to follow suit—and start clearing house.

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British politics

So much to do, so little time

Sep 29th 2005
From The Economist print edition

Nobody talks about reform more than Tony Blair. Talk is not enough

Rex Features

Get article background

"REFLECT for a moment", Gordon Brown thundered at delegates to this week's Labour Party conference, "on the talent wasted...the great music never composed, the great art never created, the great science never invented, the great books never written." The chancellor's desire to nurture all of the potential of all of the people is a wonderful thing, no doubt. But Britain would settle for much less from its government—children taught, patients treated, a pensions system that works. Yet, such is the record of Tony Blair's government, and the whiff of *fin de régime* in the air in Brighton this week, that even this is in question and no amount of vaulting ambition could conceal it.

In his own speech at Brighton, Mr Blair forsook the flourishes and blandishments that have characterised his rhetoric in the past. Step forward the "changemaker", eager at the start of his third term to get stuck into the nitty-gritty of reform. That was good politics—and welcome contrast to Mr Brown's verbal karate (see article). But it left hanging over Mr Blair one promise and two questions that will define the time remaining to him as prime minister.

The promise was Mr Blair's pledge before May's election that he would quit at some—unspecified—point in this term. It was born of weakness, when he had to pacify a rebellious chancellor who had begun to doubt that he would ever grasp the prize of becoming prime minister. The concession bought Mr Brown's co-operation, but only four months after Labour's third victory it has become a liability.

Other countries, such as America, manage just fine limiting the careers of their rulers. But in Britain, where Margaret Thatcher and Churchill hung on until they were an embarrassment to their

parties, it is an experiment—and an awkward one, because unlike George Bush, Mr Blair knows full well that his successor is sitting in the house next door. And because everybody else knows that, too, this week's conference left Mr Blair open to two awkward questions.

The uses of power

The first of these—how long can he remain prime minister?—is the one that captured the headlines. But it is the wrong question, because nobody really knows when Mr Blair will go—and he would be wise to keep it that way. Will Iraq send him packing, or next year's local elections, or his tenth anniversary as prime minister in 2007? The scheming and rivalry between the two men who have formed the most potent partnership in modern British political history have fed a small industry of comment and speculation. The prospect of his departure has given a new piquancy to the parlour game that has captivated metropolitan dinner tables for the past five years.

The second question—what can Mr Blair do with the time that is left?—is the one that matters. Mr Blair has been brilliant at winning and keeping power. His knack for dominating the centre-ground has been abetted by a self-destructive opposition. The country has suffered from Labour's hegemony. Unchallenged, his government has squandered its advantages. He frittered away his first term; in his second he spent huge sums on the public services without extracting enough concessions from workers; and over the past year he has developed an unhealthy habit of putting off difficult but much-needed reforms, whether curbing the over-generous pensions of public-sector workers or recasting local-government finances. Even Mr Blair seemed to acknowledge as much this week, when he said he regretted not taking reform further.

Those words were needed. Yet mere words from someone who finds them so easy to come by will not cut much ice. Mr Blair also needs to be seen doing something for the country—which, incidentally, would benefit his own political legacy. That means he must change his style of government.

Lessons from Maggie

His first task is to deal with Mr Brown. Cabinet ministers who have in the past looked to Mr Blair will now be planning how to carry out a deft switch of allegiance. The chancellor will want influence over the ministries so as to reach agreement with Mr Blair over reforms whose consequences will be felt throughout his own time as prime minister.

But Mr Brown is less strong than he might seem. As the economy weakens, the case for tax rises grows (see article). Moreover, the would-be prime minister can ill afford a messy transition. The chief lesson of Lady Thatcher's political demise is that parties which assassinate their leaders become introspective and factional—and develop a taste for regicide. Voters don't like that. Mr Brown's people will be awkward, but Mr Blair will be able to call his chancellor's bluff because open warfare in the Labour Party harms his inheritance more than the prime minister's legacy.

Mr Blair's other task—to change his style of government—will be harder. He is a political opportunist with a short attention span. Roy Jenkins once compared his government to a lighthouse, “its revolving beam alighting for a time on this issue or that before moving on to the next”. A man always looking to the opinion polls or the forthcoming election could not afford to overlook an attention-grabbing idea, a master plan for European economic renewal, say, or a dialogue between Islam and the West.

Now that Mr Blair no longer faces re-election, the time for grand gestures is past. The jaded

electorate has tired of extravagant promises and, even if he could convince voters of his sincerity, time is short. Mr Blair has only a year or so to make progress before the whispers mount again and so he must pick his fights and doggedly pursue them. That means, for example, forsaking illusions that he can put Britain in the European vanguard by pursuing joint reform with France and Germany.

Instead, Mr Blair should do as he says for once and get down to the hard slog of reforming education, bringing more of the market to health care, providing a coherent energy policy and reforming pensions. For a man who wants to save the world that seems a bit modest. But it is what Britain needs and what, after eight years in office, Mr Blair has failed to do.

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The Polish election

For a perkier Poland

Sep 29th 2005
From The Economist print edition

A historic chance—if the politicians take it

AP

Get article background

AT ALMOST any time in its history, the result of Poland's parliamentary election on September 25th would have seemed unimaginably good. The sheer normality of another democratic change of power is to be welcomed in a country that had until recent memory endured mostly dictatorship, autocracy and foreign rule. The ex-communists of the Democratic Left Alliance, who for four years had mismanaged the economy, slowed down reform and spawned sleaze, have been routed, winning only 11%. Fringe-party demagogues got nowhere. The two victorious centre-right parties, the populist Law and Justice and the free-market Civic Platform, broadly agree on the need to cut taxes, tame bureaucracy and break decisively with the past. Poland, you might think, weightiest among the European Union's newish entrants, would be in chipper mood, ready for a reforming fresh start.

Yet many Poles are glum (see article). Three-fifths didn't bother to vote at all—the worst turnout in the country's 15-year electoral history. Some cynicism is justified: most of the ten governments since the collapse of communism have promised clean, efficient government, yet delivered little. Why should another lot be any different? Meanwhile, rows that erupted in the final weeks of the campaign may weaken the new government. Civic Platform promised a 15% flat tax; Law and Justice derided that as a giveaway for the rich. It promised, expensively, to protect social welfare programmes.

Negotiation and compromise are not always Polish political virtues. But it is vital that politicians shed their reputation for self-indulgent squabbling. Neither party can have everything it wants. Civic Platform may have to accept that taxes will be lower, but not flat. Law and Justice should abandon populist talk of forcing the central bank to loosen monetary policy. Politicians in both parties need to remind themselves that there is much more that unites than divides them.

That is particularly true in the fight against corruption. Making good their promises to maintain high standards of cleanliness and openness would help restore sagging confidence in the political system. Views on just how to cut bureaucracy differ, yet in some areas it is obvious what needs to be done—cleaning up and depoliticising Poland's security apparatus, for example. The military intelligence agency is the country's last unreformed communist-era bureaucracy. Closing that would gladden Poland's NATO allies.

The trickiest problem, however, is how to deal with Russia. A joint approach to Russia was meant to be the centrepiece of the European Union's (supposedly) common foreign and security policy. Yet, in practice, disunity and self-interest rule. Some other European countries, chiefly Germany and France, are pursuing their own, Russia-friendly policies. The sharpest example of this is Germany's agreement to a gas pipeline under the Baltic Sea from Russia. That would allow the Kremlin to turn off the tap to Poland at will, while maintaining full supplies to western Europe.

When Poles complain loudly about Russia's heavy-handedness, as they have lately, they make it easy for Russia to portray them as paranoid Russophobes. Yet if they do not complain, nothing changes. The hard task for the new government will be to avoid the shrillness, talking politely in public, while winning allies among its European partners in private.

All good reasons for the two winning parties to sink their differences speedily. There's work to be done.

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Economics

The great jobs switch

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From The Economist print edition

The fall in manufacturing employment in developed economies is a sign of economic progress, not decline

THAT employment in manufacturing, once the engine of growth, is in a long, slow decline in the rich world is a familiar notion. That it is on its way to being virtually wiped out is not. Yet calculations by *The Economist* suggest that manufacturing now accounts for less than 10% of total jobs in America. Other rich countries are moving in that direction, too, with Britain close behind America, followed by France and Japan, with Germany and Italy lagging behind (see article).

Shrinking employment in any sector sounds like bad news. It isn't. Manufacturing jobs disappear because economies are healthy, not sick.

The decline of manufacturing in rich countries is a more complex story than the piles of Chinese-made goods in shops suggest. Manufacturing output continues to expand in most developed countries—in America, by almost 4% a year on average since 1991. Despite the rise in Chinese exports, America is still the world's biggest manufacturer, producing about twice as much, measured by value, as China.

The continued growth in manufacturing output shows that the fall in jobs has not been caused by mass substitution of Chinese goods for locally made ones. It has happened because rich-world companies have replaced workers with new technology to boost productivity and shifted production from labour-intensive products such as textiles to higher-tech, higher value-added, sectors such as pharmaceuticals. Within firms, low-skilled jobs have moved offshore. Higher-value R&D, design and marketing have stayed at home.

All that is good. Faster productivity growth means higher average incomes. Low rates of unemployment in the countries which have shifted furthest away from manufacturing suggest that most laid-off workers have found new jobs. And consumers have benefited from cheap Chinese

imports.

Yet there is a residual belief that making things you can drop on your toe is superior to working in accounting or hairdressing. Manufacturing jobs, it is often said, are better than the Mcjobs typical in the service sector. Yet working conditions in services are often pleasanter and safer than on an assembly line, and average wages in the fastest-growing sectors, such as finance, professional and business services, education and health, are higher than in manufacturing.

A second worry is that services are harder to export, so if developed economies make fewer goods, how will they pay for imports? But rich countries already increasingly pay their way in the world by exporting services. America has a huge trade deficit not because it is not exporting enough, but because American consumers are spending too much.

A new concern is that it is no longer just dirty blue-collar jobs that are being sucked offshore. Poor countries now have easier access to first-world technology. Combined with low wages, it is argued, they can make everything—including high-tech goods—more cheaply. But that's only partly true. China's comparative advantage is in labour-intensive industries; and a basic principle of economics, proven time and again, is that even if a country can make everything more cheaply, it will still gain from specialising in goods in which it has a comparative advantage. Developed economies' comparative advantage is in knowledge-intensive activities, because they have so much skilled labour. For years to come, China will be more likely to assemble the best computers than to design them.

Employment in rich countries will have to shift towards higher skilled jobs to maintain economic growth. Countries that prevent this shift taking place risk being left behind. Rather than block it, governments need to try to ameliorate the pains which change inflicts by, for example, retraining or temporarily helping those workers who lose their jobs.

People always resist change, yet sustained growth relies on a continuous shift in resources to more efficient use. In 1820, for example, 70% of American workers were in agriculture; today 2% are. If all those workers had remained tilling the land, America would now be a lot poorer.

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Central banks

An Italian comedy

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From The Economist print edition

The fiasco in Italy does not undermine the principle of independent central banks

ROPI

THERE are two men residing in Rome with open-ended tenure and near-absolute powers inside their own institutions. One is the pope. The other is Antonio Fazio, governor of the Bank of Italy. There, however, the similarities end; for, unlike the pope, Mr Fazio has been under sustained assault from all sides for his inappropriate behaviour earlier this year in adjudicating two contested takeover bids for Italian banks. Mr Fazio has simply shrugged off all criticism. He cannot be embarrassed into resigning. Central bank independence is a fine thing; but, in Italy, it has gone too far.

Last week Domenico Siniscalco, Italy's respected finance minister, himself resigned, citing Mr Fazio's outrageous tenacity as one of the reasons (the struggle to agree a sensible budget was another). Even Silvio Berlusconi, Italy's prime minister, finally found his voice and said Mr Fazio should go. In future, promised Mr Berlusconi, his government would curb the governor's role, limiting it to a term of seven years. And just in case anyone had not noticed the brouhaha, it was hard to miss the scorn of Giulio Tremonti, the new finance minister, when he joked publicly about Mr Fazio at last weekend's IMF-World Bank meeting and then sent him home, implying he was unfit to represent his country.

Yet Mr Fazio remains in his job, and his determination to ignore everyone has exposed a serious structural deficiency in the design of the Italian central bank. For decades the Bank of Italy was an island of probity in an otherwise corrupt system. Lately under Mr Fazio it has become a sick joke.

Does Mr Fazio's behaviour undermine the idea of central-bank independence? No. Central-bank independence became a reality when politicians finally accepted that it was economically foolish for them to manage interest rates—they just could not resist the temptation to try to boost growth before elections, even if this was bad policy. By setting the bankers free (and, crucially, making

them properly accountable) many countries have restrained inflation and become less prone to economic swings.

The economic case for central-bank independence remains as strong as ever—particularly in a country whose governments have tended to be corrupt, unstable or both. Yet independent should not mean unaccountable. In Italy, it does. The Bank of Italy is governed by rich charitable foundations that were set up as shareholders in the central bank partly on the proceeds of bank privatisations during the 1990s. They have links with the other main shareholders: Italy's banks, which are, in turn, supposed to be regulated by the central bank. On the evidence to date, thanks perhaps to this circular arrangement, the shareholders are unable or unwilling to stand up to a governor who is determined to hang on to office. That's daft. Central bankers should have a term limit, or an independent board to hire and fire them, or, preferably, both.

Fortunately, Mr Fazio is not really a central banker. Because Italy is in the euro zone, its monetary policy is run by the European Central Bank, not the Bank of Italy. Mr Fazio's job consists of two regulatory functions: to supervise Italy's banks (which he has done with stunning ineptitude) and to oversee competition policy in the banking sector (which Italy's main antitrust authority would do rather better). So, in effect, he is a glorified bank supervisor, whose antics have amused the rest of the world and shamed Italy but not done as much harm as if he had been a real central banker.

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On Turkey, green accounting, Anne Frank, Mexico, Hawaiian history, bra sizes

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Turkey in Europe?

SIR – Charlemagne assumes that the steps Turkey is taking towards human-rights reform (so it can join the European Union) are more than simple promises (September 17th). However, Turkey must also enforce these laws if it is serious in proving it has taken the reform path. Recent events suggest otherwise: the Greek Orthodox Halki seminary remains shut; Hrant Dink, the Istanbul publisher of the Armenian newsletter *Agos*, faces up to three years in jail for telling an audience that he is "an Armenian of Turkey"; and in March, the government defended Turkish police who attacked women during a peaceful protest. The latter event caused Gerhard Schröder to remark that Turkey's value system is "incompatible with [Europe's] common values". To promise human-rights reform is one thing, but to put it into effect is something quite different.

James Pro
New York

SIR – The idea that the ideology of Islam and its adherents in Turkey can be democratised is a pipe dream. Just look around you in any major city in Europe these days for a reality check. If Turkish immigrants cannot integrate, and voluntarily segregate into Islamic "parallel" societies, why the hopes for Turkey modernising itself? Why risk getting stuck with more such immigrants? If one is confronted with the problem of a bomb with a burning fuse the proper solution is not to swallow the bomb in order to stabilise it—one might get blown to bits that way—but rather to keep the bomb at bay.

Bas van den Beld
Utrecht, The Netherlands

SIR – Despite so-called reforms, Turkey's military maintains a decisive voice in politics, making real democracy questionable. Its military and foreign policy is slavishly pro-American and the EU does not need another Trojan horse like Britain or Italy in its midst preventing it from being a reasonable counterweight to America's unilateral interventionism. Because of its large population Turkey will insist on a decisive role, pushing founding countries like Germany and France aside.

H.S. Weiler
Cairo

Nature counts

SIR – It is better late than never for the World Bank to finally wake up to well-established thinking that the natural environment ought to have its place in our understanding of national accounts

("Greening the books", September 17th). However, the Bank's own work on structural adjustment, trade and investment fails to provide for any serious measure of social or ecological accountability. Instead, it relies on "time" to heal all wounds without regard for either the short-term consequences of its economic policies on the lives of poor people or the longer-term consequences of ecological disruption for places as far apart as the Amazon, Sahel and Mekong. One can only look forward to the greening of the Bank's own operations.

Owen Cylke
World Wildlife Fund
Washington, DC

Her story

SIR – Your review of a book on the war in Iraq refers to a young diarist as "a 14-year-old Iraqi Anne Frank" ("A grim chronicle", September 3rd). Anne Frank was not merely caught in crossfire but hunted down and murdered, along with 6m other Jews, by agents of the German state. The events of then and now could not be more different.

Ethan Taub
Zurich

Mexico's energy politics

SIR – Although your article on Mexico's presidency captured the gridlock that characterises contemporary Mexican politics, some of your recounting of recent events was confused ("A mixed record", September 10th). It was the PAN that blocked the PRI's energy proposal in 1999, and the PRI which did the same to an almost identical PAN energy plan in 2001. Moreover, the energy bill vetoed by President Vicente Fox early last month, which proposed less taxes for Pemex (the state oil company), was very different from the 1999 and 2001 proposals, which called for the electricity sector to open up to private investors.

Cesar Hernandez
Centre of research for development (CIDAC)
Mexico City

Trouble in paradise

SIR – Your understanding of Hawaiian history is wrong ("Sun, surf and secession?", September 3rd). Queen Liliuokalani was not overthrown in 1893 by "local rebels", but by *haole* planters. And thousands of Hawaiians signed a petition in 1898 protesting the annexation by the United States. Moreover, you entirely missed the point over what is currently at stake in Senator Daniel Akaka's "self-governance" bill for native Hawaiians. This is about land that has eventually passed from the Hawaiian kingdom to people with Hawaiian ancestry. Most of this land is now held in trust by state and federal government. This is a very different issue to the governance of the whole state of Hawaii, which you imply is the bill's basis.

John Fleckles
Kaneohe, Hawaii

SIR – It was at the request of American businessmen that John Stevens, the American minister to Hawaii ordered a contingent of marines from the *USS Boston* to occupy the palace and other government buildings. Liliuokalani yielded her authority under protest, but asked people to observe the rule of law and not to shed blood, which explains why her subjects did not even "fire a

single shot in her defence". By the way, it was Congress, and not Bill Clinton individually, which apologised 100 years later to native Hawaiians for depriving them of the right to self-determination.

Charles Ke'aumakalani Richards
San Francisco

SIR – Your misinformed interpretation of Hawaiian history was so off base that I'm surprised you didn't refer to Hawaii as the Sandwich Islands.

Saara Dutton
New York

SIR – I am an American of Hawaiian, Chinese and Filipino ancestry and was born, raised and have lived in Hawaii my entire life. Because of my Hawaiian ancestry, the Akaka bill would grant me special privileges, entitlements and tax-free benefits that my Filipino and Chinese cousins would not receive. But I still oppose this legislation. Some of the darkest chapters in human history were written by governments that discriminate in favour of some, but against others, based on race. The Akaka bill would turn us down that dark path. It would force separatist tribalism upon the most racially integrated state in the world. You are correct: that any politician would be in favour of this legislation is truly amazing.

Sandra Puanani Burgess
Honolulu

Sizing up a situation

SIR – I read with interest your leader on Europe's problems with a backlog of imported Chinese bras ("Storm in a D-cup", September 10th). But I could not help wondering what Freudian reason caused the writer of your headline, when both the letters B and C also rhyme with "tea", to choose the D-cup?

Krishna Prasad
Toronto

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Poland

Can the eagle soar?

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Poland's election result offers the chance of much-needed change in the European Union's biggest ex-communist country

Get article background

FROM afar, the Polish eagle is an impressive sight: a strong ally to its western friends, particularly America, and an inspiration to its eastern neighbours in places like Ukraine where economies are sagging and democracy wobbly. The media, from serious magazines to zingy tabloids, are truly eagle-eyed, and the envy of other post-communist countries. The eagle is brainy too: since the collapse of communism in 1989, the number of students has risen fivefold, to 2m; never before have Poles been so well educated. In short, Poland has never been so democratic, so secure and so prosperous.

Yet from close up, the Polish eagle looks tatty, tired and tied up in red tape. The centre-right parties, the populist Law and Justice and the free-market Civic Platform, that won last Sunday's election face a huge task if they are to spruce Poland up and unleash its full potential.

The big point is that, for all Poland's successes, other former captive nations are doing even better. Most beat Poland's annual growth rate, which is 2.8% and slowing. Some, such as the Baltic states, are growing three times as fast. That is partly due to foreign investment—a contest in which Poland has been falling behind. Investor-friendly Slovakia has done much better in winning big auto plants. But it is true in other bits of life too: Estonia, for example, is streets ahead in making the state administration lean and business-friendly. Although individual Polish firms and their workers are still highly competitive, their country, increasingly, is not.

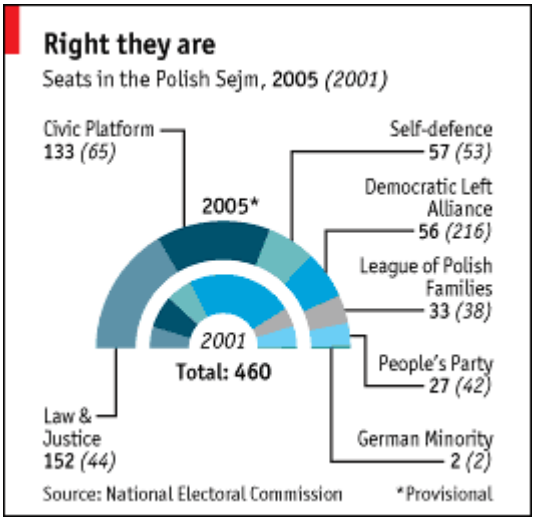
Part of the problem is that the outgoing government, run mainly by ex-communists, was bad at both raising money and spending it. The tax system is complicated, riddled with exemptions and

pitfalls, and tough on the most productive (the top marginal rate of income tax, widely evaded, is 40%). Big social charges levied on salaries make it expensive to create jobs—to put the equivalent of $100 in cash in a worker's pocket, an employer must pay well over $200—and unemployment is 18%.

To match that, government spending is poorly targeted and wastefully administered. Politically influential groups, such as miners, have been given hugely expensive early retirement deals. Officials drive shiny new cars to their shiny new offices. But inside, the wheels of state are rusty.

One result is that Polish public finances are in a mess. Including debts to private pension funds, the budget deficit is 6.8% of GDP. The debt-to-GDP ratio is 53%, perilously close to the constitutional limit of 55%. Once that is exceeded, drastic mandatory spending cuts and tax rises kick in. To make up for loose fiscal policy, monetary policy is tough: real interest rates, at 5.5%, are three times the rate of inflation.

That adds to the costs borne by Poland's businesses. So does the bad infrastructure. Most Polish main roads (and many Polish drivers) are dangerous by developed-world standards. Only 3% of main roads meet EU rules; Poland's motorway density (kilometres per 1,000 square kilometres) is one-sixth of other central European countries'. Road fatalities, at around 5,500 a year, are about the same as in Spain—despite a much lower level of car use and ownership. That throttles the movement of goods and people: a journey that in a western country would be an uneventful 90 minutes is a hair-raising three hours plus, dodging horsedrawn carts and potholes on narrow, twisting roads.



That, at least, should be easy to fix—but for the Polish bureaucratic culture of quarrel and delay. Generous EU aid is transforming roads, bridges and the like in other new member states. But in Poland the process is painfully slow. “To build a big new road you need to get agreement from the different bits of local government involved, and from the ministry,” explains a lawyer familiar with the process. “Only when they have got everything signed and sealed do you get the EU money. And all too often they just squabble.”

Comfy cartels and dotty rules

Past governments have also been very weak in encouraging the intensified competition that raises standards and creates jobs. Though the first Polish post-communist government invented the idea of “shock therapy”, the results were so bruising that Poles have been shy of radical economic change ever since. The result has been an encrustation of crony-led cartels, particularly in big formerly state-owned industries. Telecoms services are, on average, twice as expensive in Poland as in competition-loving Estonia.

That keeps Poland poor in one way. The endless petty burdens on business—a lethal combination of badly-drafted rules and badly-run bureaucracy—destroy jobs and wealth in another. Take, for example, the rules about holidays. It is reasonable, perhaps, for the state to say how many days holiday workers must receive each year. But Poland goes further, with a paternalistic rule that at least ten working days must be taken together. That stops flinty-hearted employers parcelling out days off in inconvenient dribs and drabs: all employees get an uninterrupted two-week break. But what if they don't want it?

At PMR, a business-information company in Cracow, staff asked their bosses not to implement this rule; they wanted to be able to take their holiday as it suited them. The company agreed, and even managed to obtain a letter from the labour inspectorate giving broad agreement. But the company's lawyers gave warning that this would be no defence in law. By allowing employees to do as they wanted, the company risked a 5,000 zloty ($1,500) fine.

That kind of thinking stems from opposition trade unionism in the communist era. In a planned economy (which typically put workers' interests last) fighting for every possible bureaucratic bastion for workers' rights was rational. When communism fell, the victorious trade unionists of Solidarity rewrote the lawbooks, giving Polish workers detailed, prescriptive legal protection, of a kind that now looks pointless and out of date.

In practice, with a bit of nerve, time and ingenuity, many rules can be dodged. A firm must by law have a physical (not electronic) file on every worker. Another Cracow technology company tracks its employees' activity using modern software, but keeps a paper-based system recording an entirely bogus reality where everyone arrives at 0800 and leaves at 1600.

The real routine—enthusiastically accepted by the well-paid staff—breaks both daily and weekly statutory limits on hours worked. But that's not the point. The harried manager explains, “When respectable executives in respectable companies are forced by lunatic legislation to break the law because it is impossible to run the company legally, they have to focus on issues that have nothing do to with competitiveness or adding value. It is extremely demotivating. Plus respect for politicians and administration crumbles and ‘thin end of the wedge' issues arise—if we are breaking some laws, where do we stop?”

The most conspicuous weakness of all is in the judicial system, which, according to the American Chamber of Commerce in Warsaw, is “grossly inefficient”. Resolving a lawsuit about a contract takes, it reckons, an average of 92 months. The law and the system that enforces it go to great lengths to protect debtors, but care little for creditors. That thinking may have a spurious air of fairness about it, but it imposes real costs for businesses, which in many cases can choose countries where the legal environment is more friendly. There are other changes needed too: judges are underqualified and ill-trained and work in archaic offices; courts are underequipped and burdened with jobs, such as running property registers, that they do badly.

Diagnose, prescribe, treat

These are all common problems in the post-communist world. The odd thing about Poland is that a country bursting with oomph and ambition, and with some highly intelligent politicians, has been so bad at dealing with them. Polish politics over the past 15 years has been a bewildering, and mostly depressing, cavalcade of short-lived governments and short-term fixes. Rather than get on with the nitty-gritty of running Poland better, politicians have preferred to indulge in rows about the past.

It is easy to see why. Anti-communist Poles find it deeply frustrating that the hated relics of the totalitarian era have not only escaped prosecution, but in many cases have managed to turn old commie connections into new capitalist wealth. Why should honest patriotic Poles be poor, when crooked treacherous collaborators are rich?

A second great cause of grievance is the loosely sealed files of the communist-era secret police. Unpleasant surprises from these drip out piecemeal. One politician recently discovered, just before his sister's wedding, that her much-loved godfather had been spying on the family for many years. “What am I supposed to do” he asks. “Tell her, and ruin her wedding, or allow this bastard to come as if nothing had happened?” The demand to open the archives once and for all was one of

the most popular parts of the election programme of Law and Justice. It talks of creating a “Fourth Republic”, to draw a line under the tainted “Third” republic that dates from the collapse (but not eradication) of communist Poland in 1989.

There are gripes on the other side too. Those who did well under the communist regime resent the arrogance and self-righteousness of their adversaries. Rather like the French resistance, they argue, the valiant seem a lot more numerous since victory. And why should those people who made money in the early years of post-communism be penalised for having the connections and nerve to turn a profit. Surely that's what capitalism is all about?

These arguments have raged for 15 years. Now they are ending, thanks to the near-collapse of the main ex-communist party, the Democratic Left Alliance. It reached its high point under the two-term presidency of Alexander Kwasniewski, a suave, savvy politician with a background in Poland's communist-era youth movement. He gained increasing, if grudging, cross-party respect at home, and enthusiastic praise abroad, for his statesmanlike ways—helping broker the deal that changed regimes in Ukraine last year was a particular triumph.

But Mr Kwasniewski is in his last few weeks as president: Poland will elect a new head of state on October 9th, with a run-off two weeks later. That will be a contest between Donald Tusk from Civic Platform, and Lech Kaczynski from Law and Justice. The ex-communist candidate, the smooth-talking but thin-skinned Wlodzimierz Cimoszewicz, was entangled in a corruption scandal and had to withdraw from the race in September. That set the scene for last weekend's parliamentary elections in which the ex-communists were trounced, gaining only 11% of the vote, compared to 41% in 2001.

Internecine war

In the long term, the near-death of the ex-communists is excellent news. It clears the way for a modern centre-left party, unburdened by the baggage of totalitarianism. And it means that centre-right politicians no longer have the luxury of bashing an easy target. In the short term, however, it has prompted the anti-communist parties to bash each other.

The final weeks of the election campaign were a dismaying experience for reform-minded Poles. Law and Justice launched a fierce attack on its rival, Civic Platform, caricaturing it as a party that stood for the interests of wealthy businessmen. That shrivelled Civic Platform's poll rating, once nearly double that of Law and Justice. When the votes were counted, Law and Justice was ahead, by 27% to 24%.

That was not the expected result. Civic Platform's lead had seemed so unassailable that fans had started calling its candidate, Jan Rokita, “Mr Prime Minister”. It seemed likely that Civic Platform would head the government and run the economy—its strong point—while Law and Justice would have ministries such as justice and home affairs where its fierce moral sense would fit well.

Now things look a lot more complicated. Mr Kaczynski's twin brother, Jaroslaw, has dropped his claim to the prime minister's job, at least until after the presidential election. Instead, Law and Justice has put forward Kazimierz Marcinkiewicz, a colourless, cautious figure with a background in hardline Catholic politics. He is now trying to negotiate a government programme with Civic Platform. Only then will ministerial portfolios be allocated, he says. That means weeks of uncertainty. But the danger is that even when the new government forms, it will be a marriage of convenience rather than a real alliance.

In particular, some people in Law and Justice are suspicious of Civic Platform's integrity. Although Mr Rokita and Mr Tusk are seen as honest beyond criticism, there are question marks over some

party pals and advisers. In turn, Civic Platform's people think that Law and Justice are at heart collectivists, in the tradition of pre-war Poland's anti-communist Socialist party. They also dislike the party's socially conservative agenda. Its presidential candidate, Mr (Lech) Kaczynski, is the outgoing mayor of Warsaw. In that job he attracted criticism from the liberal-minded (and praise from traditionalists) for banning a gay pride march. Limited intellectual horizons are an easy target too. For example, Mr Kaczynski still refers to “Chancellor Kohl” of Germany and has declined almost every opportunity to take trips abroad. If Law and Justice influences Poland's foreign affairs stance strongly, it will mean an insular, stroppy, nationalist tone.

The fundamental problem is that the two parties appeal to very different electorates. Civic Platform's support is overwhelmingly in the booming, mainly western parts of Poland (see map); in big cities, and among younger and better-educated Poles (among students it won a whopping 41%). Law and Justice was competing for votes with populist and ex-communist parties in poorer, rural parts of society.

In the long term winners are outnumbering losers, so Civic Platform is well-placed. But for now, the two parties are pulled in different directions. Law and Justice reflects the anger of losers from the past, who want social justice, shared prosperity and protection for the weak against the strong. Civic Platform is the party of the impatient, globalised elite, which wants Poland to be the most competitive economy in Europe—even at the price of greater inequality and dislocation.

That should not be insurmountable. The differences between the parties are far less than those within single governing parties in other countries—such as Britain's Labour Party. When the political will to govern is there, arguments lead to compromises and decisions. But there is precious little tradition of that in Poland. Every right-of-centre government so far has bickered and

split. The two parties should now be aiming to get a government that more or less works, rather than the dream team that some were hankering for.

Snipping not slashing

That will mean little chance of the new government attacking Poland's problems head-on with a radical, comprehensive programme of reform. Red tape will be snipped, rather than slashed. Reform will be piecemeal. Change will depend on which minister gets which portfolio, rather than being pushed hard on every front by a government with big ideas.

That is sad, but it is not a catastrophe. Poland is lucky that its fundamental competitive advantage is so strong: with average wages of $670 a month, the room for more investment and more exports is huge—even though progress would be still faster under a more focused government.

The most important task for Poland's new rulers will be to make sure that they govern for a full term, without splits or scandals. An interesting feature of the election result is that the populist parties, the right-wing League of Polish Families and the left-wing Self-defence, were not wiped out. Together with the ex-communists, they will form a disparate but probably effective opposition. With almost all the sensible politicians in the government, any alternative administration is bound to look alarming. In short: if this government fails, watch out for what comes next.

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The conservative movement

A Hammer blow

Sep 29th 2005 | AUSTIN AND WASHINGTON, DC
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AFP

The indictment of Tom DeLay may not be the start of a conservative crack-up; but it could mark a realignment

TOM DELAY is no stranger to excitement. He claims nearly to have been killed during a bout of revolutionary violence in Venezuela, where he lived in his teens. He was asked to leave the first university he attended, and he made a living exterminating bugs before he entered politics. But "the Hammer" has not been able to swat away the swarm of investigators buzzing around him.

On September 28th, Mr DeLay was indicted by a grand jury in Texas for alleged breaches of campaign-finance law, and forced to resign, at least temporarily, his position as Republican majority leader in the House of Representatives. There was much whooping among Democrats, for whom Mr DeLay was a hate figure even before he played a crucial part in the impeachment of Bill Clinton. "I hope his cell is full of cockroaches," was one of the gentler postings on one leftish blogsite.

Washington, DC, is now engulfed in two debates. The first revolves around how bad a mess Mr DeLay is in; the second is about the extent of the fissures within the conservative movement that currently dominates American politics.

The case against Mr DeLay is less easy to understand than the perjury-about-fellatio charge against Mr Clinton. Along with two political associates, John Colyandro and Jim Ellis, he is accused of conspiracy to violate the election code in his home state of Texas. Mr DeLay has a political action committee called Texans for a Republican Majority (TRMPAC). Prosecutors allege that it accepted $155,000 from various companies, and then wrote a cheque for $190,000 to an arm of the Republican National Committee, with instructions to distribute chunks of the stash to individual

candidates in Texas. In effect, the indictment argues, TRMPAC enabled the party to get around the ban on corporate donations to individual candidates.

If convicted, Mr DeLay faces up to two years in jail and a fine of up to $10,000. But that is far from certain. He has denounced the charges as “one of the weakest, most baseless indictments in American history”, adding that the district attorney behind the case, Ronnie Earle, was “an unabashed partisan zealot with a well-documented history of launching baseless investigations and indictments against his political enemies”.

Mr Earle is a liberal Democrat who, in 1993, indicted Kay Bailey Hutchison, now the state's senior Republican senator, on what “The Almanac of American Politics” called “flimsy charges he was forced to drop the first day the case came to court”. Against that, Mr Earle has prosecuted four times as many Democrats as Republicans.

Mr DeLay said that his defence “will not be technical or legalistic; it will be categorical and absolute. I am innocent. Mr Earle and his staff know it. And I will prove it.” He then promised that Republicans would not be deflected from their “bold and aggressive agenda” to do something about petrol prices, state pensions, illegal immigration and fiscal responsibility—issues he vowed would all be tackled in the next few weeks.

That may be a bit optimistic. For one thing, the Republicans will miss Mr DeLay's vote-whipping skills. He has a startling record of assembling hair-thin majorities for ticklish pieces of legislation, such as on Medicare prescription-drug benefit in 2003. In other words, he is adept at offering the necessary inducements to just enough waverers, but no more.

His case will probably not come to trial for several months, and in the meantime he remains a member of the House of Representatives. His duties as majority leader are to be assumed, for now, by Roy Blunt of Missouri, the House Republican whip, with assistance from David Dreier, a representative from California, and Eric Cantor of Virginia. None is likely to be as forceful as the Hammer.

Mr DeLay's indictment is not the only ethical problem hampering the Republicans. Bill Frist, the Senate majority leader, is being investigated about a stock sale he insists involved no inside information. Karl Rove, Mr Bush's chief strategist, is fighting accusations that he leaked the name of Valerie Plame, an undercover CIA agent. And Mr DeLay's problems are not limited to Texas: a lobbyist chum of his, Jack Abramoff, has been accused of a variety of dodgy doings involving Indian casinos and influence-peddling.

This accumulation of sleaze has made it harder for the Republicans to push through their agenda, reckons Thomas Mann of the Brookings Institution, a liberal think tank. Other pundits are not so sure. Norman Ornstein of the American Enterprise Institute, a conservative think tank, says Mr DeLay's indictment will “not have a huge impact” on the Republican legislative programme, “mostly because it was in tatters before”.

That might sound odd. After all, only last November conservatives were preening themselves like peacocks, having won their seventh presidential election in ten contests. Mr Bush ran for his second term on a conservative platform of tax cuts, family values and American power. Marshalled by Mr Rove, millions of activists—anti-tax people, gun people, social conservatives, neo-conservatives and many more—comprehensively outfought their liberal equivalents. Mr Bush won more votes than any candidate in history.

Today the conservative movement is in turmoil. Different types of conservatives are at each other's throats. Everybody is hurling opprobrium at the president. David Brooks, a conservative columnist on the *New York Times* recently declared that he sometimes wonders whether Bush is a

Manchurian candidate—sent to discredit conservatism.

The loudest howls are coming from small-government conservatives who are furious with Mr Bush's loose spending (see article). But business conservatives are furious about his love-affair with the religious right and traditional conservatives are furious about his commitment of blood and treasure to the Iraq war.

These rows are particularly dangerous because they reflect long-standing tensions within the conservative movement.

•**Small-government conservatives v big-government conservatives.** Mr Bush has embraced all sorts of big-government programmes (from super-charging the Department of Education to creating the huge new Medicare drug entitlement) while trying to keep small-government conservatives on side with tax cuts. But this was a formula for fiscal disaster. It also failed to placate purists who believe that the federal government has no business running schools or pushing pills to pensioners.

•**Conservatives of faith v conservatives of doubt**. Doubters don't think that the federal government should interfere in people's private lives. They don't want Washington, DC, meddling in states' rights to legalise euthanasia or medical marijuana. Conservatives of faith believe that the federal government should encourage civic virtue. Under Mr Bush they have had the upper hand. The Justice Department has been aggressive in imposing its views on the states. The poster child of the conservative movement on Capitol Hill at the moment is Senator Rick Santorum, a staunch advocate of family values.

•**Insurgent conservatives v establishment conservatives.** The conservative movement, rooted in the South and west, has been deeply hostile to Washington, DC. But electoral success has created a Washington-based Republican establishment, which spends its time doling out goodies to its buddies and expanding federal power. Mr Bush has managed this relationship by presenting himself as an anti-Washington Washingtonian: the son of a president who prefers to spend his time in Texas. The insurgent wing seems increasingly unconvinced.

•**Business conservatives v religious conservatives.** The latter are waiting keenly to see whom Mr Bush appoints next to the Supreme Court. Business conservatives are worried that religious people have already got too much. Mr Bush's stance on stem-cell research will cost America its competitive edge in biotechnology. Add to this their concerns about Mr Bush's reckless fiscal policy and you have the making of a business revolt. Robert Novak, a conservative pundit, recently described a cacophony of Bush-bashing at a plutocratic get-together in Aspen.

•**Neo-conservatives v traditional conservatives**. The former have an expansive vision of America's role in the world—a vision that has come to include not just nation-building in Afghanistan and Iraq but also the transformation of the Middle East. But traditionalists balk at the hubris of this vision. How can conservatives who believe that government power is fallible rally to the idea of transforming an entire region?

This sort of criticism was once limited to mavericks such as Pat Buchanan. But it is now mainstream. William Buckley, one of the movement's founders, has declared that the Iraq war was probably a mistake. Before the election, one senior White House figure confided that his biggest worry was not the anti-war left (which always sings the same song) but the possibility that the conservative intellectual elite would turn against the war. The *rive droite* seems to be turning.

How bad is this? All successful political parties contain tensions. Look at Britain's Labour Party—a party of pacifist trade unionists led by a hawkish fan of capitalism. The bigger a political party gets, the bigger the tensions. Politics is the art of managing these tensions—something Mr Bush's

team did brilliantly until this year.

The loss of touch began before Hurricane Katrina. Bungling in Iraq provoked a drumbeat of discontent, with neo-conservatives calling for more troops and traditional conservatives calling for an exit strategy. And the Valerie Plame affair demoralised the White House. It not only threatened Mr Rove's political career; it also demonstrated how far Mr Bush's pursuit of the war had alienated much of the Washington establishment (including the CIA and the State Department).

Getty Images

Can Rove turn it around again?

Katrina has been a disaster. Mr Bush's slow response to the hurricane (it did not help that Mr Rove was in hospital) spoiled his claim to be a can-do president and it unleashed a previously quiescent press.

The Bush machine's ruthless media management infuriates journalists, but while he was on top they played the game on his terms. Now they are out for revenge. Earlier this year, *Newsweek* fawned about the “hands-on and detail oriented” president who wants to hear the bad news first. After Katrina it presented a picture of a man who surrounds himself with toadies who are too terrified to warn him of brewing disaster. Mr Bush cannot even rely on the conservative press to leap to his defence; they are too busy berating him for spending like a Democrat.

Surviving Watergate and Bill Clinton

Predictions of the demise of American conservatism are almost as old as the movement. It survived both Watergate and Bill Clinton. Emmett Tyrell, the editor of the *American Spectator*, published “The Conservative Crack-up” in 1992. David Frum published “Dead Right” on the eve of the Republican takeover of Congress. So much of the right's power lies outside the administration and Congress—in its domination of the intellectual agenda for instance—that it is seldom down for long.

The Democrats show few signs that they have the wind in their sails. Their handling of John Roberts's nomination to the Supreme Court has been dismal. Neither Harry Reid, the minority leader in the Senate, nor Nancy Pelosi, the minority leader in the House, are likely to set the world on fire. Moveon.org types want to drag the party to the left; Clintonistas want to pull it to the centre. America has two dysfunctional parties.

But Mr Bush's recent problems do raise one important possibility: that of a realignment on the right. The fact that the Bush machine is running out of steam makes it much less likely that he will be able to determine his successor. This creates opportunities for very different sorts of conservatives who are waiting in the wings.

One possibility is Rudy Giuliani, who combines managerial toughness with social liberalism. But an even more likely one is John McCain. Up until now Mr McCain has been popular in the country at large (he wins all head-to-head competitions with Hillary Clinton) but unpopular with the conservative movement. But the right is beginning to warm to him. He has spent his career campaigning against the sort of pork-barrel spending that conservatives are now railing against. And he is soundly conservative on both foreign and fiscal policy. A conservative crack-up may be going too far; but a conservative realignment is definitely in the works.

Economist.com WORLD NORTH AMERICA

The fiscal mess

Or is it an opportunity?

Sep 29th 2005 | WASHINGTON, DC
From The Economist print edition

A useful battle about the budget is raging within the Republican Party

THE winds were slower than feared, while the government response, by and large, was surprisingly competent. As a result, Hurricane Rita wreaked less havoc than many expected (see article). But a storm is raging in Washington, DC, over the fiscal consequences of hurricane relief. Nowhere more so than within the Republican Party.

The past couple of weeks has seen a near revolution among conservative Republicans, who are apoplectic about Mr Bush's promise to spend "what it takes" to rebuild New Orleans while making no effort to pay for that spending with cuts elsewhere. They are also furious with their leaders in Congress. Well before he temporarily resigned as House majority leader, Tom DeLay had riled conservatives by claiming the budget was "pared down pretty good". True believers in small government were incredulous, pointing out that George Bush has outspent every president since Lyndon Johnson.

The Republican Study Committee, a group of 110 conservatives in the House, quickly found more than $500 billion worth of cuts over ten years. Many were well-worn political footballs, such as cutting foreign aid or subsidies for railways. But others—including postponing the date when Medicare starts paying for pensioners' prescription drugs by a year (which would save $30 billion), or cutting some of the most egregious pork from the recent bacon-filled highway bill—found a new echo across Republican ranks.

John McCain, the pork-bashing senator from Arizona who still wants to become president in 2008, offered his own set of fiscal offsets, including clamping down on the growth of spending outside defence and homeland security. A few moderate senators even muttered about revisiting the Bush tax cuts. Jeff Flake, a congressman from Arizona, wrote in the *Wall Street Journal* that "the Republican Congress's failure to discipline itself is sending us all down a flower-strewn path to financial insolvency".

And the complaints went well beyond Capitol Hill. Right-wing think tanks published blistering criticisms of the spending binge. In many ways the hurricanes are an odd catalyst for this bout of Republican fiscal angst. Even if the reconstruction ends up costing $200 billion, that is a one-time cost of less than 2% of GDP, a mere blip on America's long-term fiscal path, and—as many Democratic economists are quick to point out—rather less than the annual cost of Mr Bush's tax cuts.

So why are conservatives suddenly so concerned? The Katrina spending binge has come only weeks after the highway bill, which already had them hopping. Mr Bush promised that he would not allow the highway bill to cost more than $256 billion. Yet he merrily signed a package that cost $286 billion and which reeked of pork, including $223m for one Alaskan bridge to reach a community of 50 people and another $231m for a second bridge to a place where nobody lives. How could Mr DeLay claim there was no fat to cut when he just voted for a bridge to nowhere?

The big question, of course, is whether this harrumphing actually leads to any change in America's budget policy. Could this be a tipping point? The early signs are no, but there may be some effect on reconstruction spending.

The $200 billion estimate for the costs of Katrina could well be far too high. One top budget wonk on Capitol Hill this week said he thought $100 billion was a more realistic figure. So far only a fraction of the $70 billion that Congress has already appropriated has actually been spent. And some of the new requests are so outrageous that they may provoke a backlash. Louisiana's lawmakers, for instance, have asked for $250 billion for their state (or more than $50,000 per inhabitant).

But despite the conservatives' ranting, neither the White House nor congressional leaders have offered any concrete spending cuts. Mr Bush has told his boffins to look for savings, but with little urgency. Top lawmakers are busier lecturing the conservative renegades about the need for party unity.

Political jitters suffuse this debate. Republicans are all nervous about Mr Bush's low poll ratings and their own prospects in the 2006 mid-term elections. But they draw different conclusions. Conservatives fear that their base will punish a party that is no longer the champion of small government. Congressional leaders fear that cutting programmes which help the poor (such as Medicaid), let alone putting off a broader and long-promised middle-class benefit (Medicare prescription drugs), are surer vote killers.

Judging by the polls, Americans think that there should be some sacrifices to pay for Katrina expenses. But their targets are not those of the Republican right. According to a recent Associated Press poll, four out of ten people thought America should spend less in Iraq to pay for Katrina. Almost three out of ten think some of the tax cuts should be cancelled or delayed. Only 11% would cut other domestic spending.

Democrats have notably failed to join the right's backbench revolt. Nancy Pelosi, the top Democrat in the House, scored some points by offering to give up the $70m in special projects her district had been promised by the highway bill. But no Democrats are seizing the opportunity to focus more broadly on fiscal discipline. Democrats worry any subsequent spending cuts will hurt their constituencies most. They fret, with some reason, that Republican-inspired spending cuts would focus on Medicaid, food stamps and other government programmes for the poor.

Democrats are also nervous about pushing hard for tax hikes. Take, for instance, the eliminations of the personal-exemption and itemised-deduction phase-outs. These two tax-cuts were included by Congress in Mr Bush's 2001 tax package and are set to begin in 2006. For Democratic politicians these eliminations ought to be a perfect target: they have not yet taken effect, their benefits accrue to the richest Americans, Mr Bush did not even ask for them, and, according to Jason Furman of the left-leaning Centre on Budget and Policy Priorities, their long-term cost is approximately $200 billion. Yet the politicians remain leery. Unless Democrats show some courage, the Republican fiscal storm will blow out.

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After Hurricane Rita

Chaos on the coast and on the Hill

Sep 29th 2005 | HOUSTON, NEW YORK AND PORT ARTHUR
From The Economist print edition

And the hurricane season isn't finished yet

WITH its giant refineries, Port Arthur, Texas, is an eyesore at the best of times. Hurricane Rita has made it worse. The roof at Sanders Collision Centre has fallen in, burying a shiny red pick-up truck. A furniture truck lies half-overturned in a driveway. Trees have toppled into telephone poles. Memorial Boulevard, a city thoroughfare, dead-ends in water.

Still, the Gulf coast got off lightly. The giant hurricane struck Texas and Louisiana last weekend with 120mph winds. That is horrific, but down from the 165mph lashing that had been feared. Louisiana, still reeling from Hurricane Katrina three weeks ago, saw more flooding and is seeking billions more in aid.

With the cluster of refineries along the Gulf not seriously damaged for the most part, America avoided petrol catastrophe. But Rita will have an impact at the pump. At mid-week, nearly all of the Gulf of Mexico's oil production and most of its gas production was still shut down. Some guess that Rita may have damaged more rigs than any hurricane in history. And that comes after Katrina, which also pounded the region's underwater pipelines, and left several refineries under water.

With retail petrol prices rising, George Bush was forced to encourage Americans to “curtail non-essential travel” and to car-pool when possible. He announced that he was willing to release crude

oil from the government's Strategic Petroleum Reserve once again, as he had done after Katrina. The hitch is that the shortage is not in crude but in refining capacity and in petrol, for which America has no strategic stocks. He also talked of easing environmental regulations and encouraging new refineries in other ways (the last one opened in 1976), a topic taken up with gusto by Congress.

Like officials at every level following the Katrina debacle, Mr Bush certainly prepared better for this storm. He made a show of monitoring the weather at the Northern Command Centre in Colorado, after getting flak for fiddling while New Orleans flooded. The National Guard and Federal Emergency Management Agency (FEMA) teams were in place early, and officials lined up plenty of buses to evacuate the homeless and helpless. Tragically, one bus exploded near Dallas, killing 23 nursing-home residents. New Orleanians, many of whom sought refuge in Houston after Katrina, hit the road again.

But even the best-laid plans go wrong. It turns out that New Orleans and Houston are very different cities. In New Orleans, officials forgot that plenty of poor people had no transport. In Houston, America's fourth-largest city, everyone seems to have had a gas guzzler. Hundreds of motorists fleeing the massive storm had to abandon their cars after petrol stations ran dry. It was, said a *Houston Chronicle* columnist, “the largest automotive jam in world history.” Many vowed never to heed another evacuation call. “We're taking sleeping bags and bunking down in the hallway [next time],” says Laura Calaway, a Houstonian mother of two. Her family took nine hours to drive 70 miles.

Then there was the problem of getting back. This went more smoothly, though it is unclear how many people heeded authorities' calls for a staggered re-entry (northwest Houston returning Sunday, south-west on Monday, etc). East of Houston, many petrol stations remained shuttered. Roger Ross, a Port Arthur resident who stayed through the storm (and helped your correspondent when her tyre got busted by hurricane debris), complained that police tried to stop him from re-entering when he sought petrol. “It's crazy,” he said of being forced to sneak home.

Meanwhile, recriminations from Katrina rumble on. The police superintendent of New Orleans resigned this week, his force shrunken by desertions. In Washington, DC, Michael Brown, FEMA's former director, made his first appearance before Congress to give his side of the story.

The congressional investigation was set up by the Republican leadership in the House, but boycotted by the Democrats who wanted an independent commission (as do 80% of the American people, according to a Gallup/*USA Today* poll). Mr Brown was combative. His biggest mistake, he said, was “not recognising by Saturday [shortly before the storm struck] that Louisiana was dysfunctional.” Mr Brown heaped blame on Kathleen Blanco, Louisiana's governor, and another Democrat, New Orleans's mayor, Ray Nagin.

That went down well with his Republican inquisitors. They seemed less satisfied by his repeated insistence that FEMA's job was just co-ordinating disaster response, not ordering evacuations or handing out petrol. He lashed out at the media and insisted he was well qualified for directing the agency (notwithstanding his fabled past as an Arabian-horse expert).

Mr Brown's successors aren't doing well at avoiding controversy. FEMA's promise to reimburse faith-based groups who housed and fed New Orleans evacuees at the government's request has drawn ire from civil liberties groups. And other claimants are lining up. Texas's governor wants Rita and Katrina to be considered a single disaster, so the state can claim 100% of the cost of Rita from the federal government too. And, remember, the hurricane season still has two months to run.

Arnold Schwarzenegger

Samson shorn?

Sep 29th 2005 | LOS ANGELES AND OAKLAND
From The Economist print edition

The prospect of a disastrous special election—and a rival from Tinseltown

Get article background

IS THE Gubernator about to suffer political humiliation? On November 8th, California's voters will be summoned to a special election—and, if the opinion polls are right, they will rebuff most, if not all, of the ballot initiatives Arnold Schwarzenegger deems essential for his "year of reform".

Mr Schwarzenegger launched his campaign in January as an admirably bold bid to fix California's budgeting system. This is a mess thanks to two things: spending increases mandated by the voters; and a legislative stalemate between a Democratic majority that wants to protect public programmes and a blocking Republican minority that refuses to raise taxes.

Originally, the governor's plan included measures to privatise much of the state pension system and to link teachers' pay to their performance. Those have been dropped, leaving four initiatives: Proposition 74 would make teachers wait for five years, instead of two, before being confirmed in their jobs; Proposition 75 would require public employees' unions to have the written consent of individual members before making political contributions; Proposition 76 would put limits on state spending; and Proposition 77 would make the drawing of constituency borders the job of retired, independent judges instead of self-interested lawmakers.

Terminated?
Voter support, %

	Jun 2005	Aug 2005
Proposition 74	61	46
Proposition 75	57	55
Proposition 76	35	19
Proposition 77	35	32

	Feb 2005	Aug 2005
Second term for Arnold Schwarzenegger	56	36

Source: Field Poll

According to the Field Poll, only Proposition 75 enjoys majority support (see table). And the unions have overturned similar measures before. Mr Schwarzenegger, of course, has a similar record of winning in the end. But he has left it awfully late in the final reel for a heroic counterattack.

For months on end, California's public employees' unions have savaged him in TV commercials, accusing him of being in bed with big business. Their well-organised demonstrators have dogged his public appearances; and, as one attack follows another, they have driven his approval rating from 55% in February to a mere 36% as of late August. Only now is the erstwhile Terminator fighting back—and only with low-key TV-ads, tame "town hall" meetings and a belated attempt to repair relations with Latinos.

Another tactical mistake surely was to label California's hard-pressed and generally popular nurses, teachers and firemen as "special interests" whose butts he would take pleasure in kicking. The unions have collectively spent around $60m lobbying against ballot measures that would reduce their power. But this is a Republican governor whose fund-raising has outpaced even that of Gray Davis, his unlamented Democratic predecessor (at one Schwarzenegger dinner last year in

New York, the star-struck were invited to contribute up to $500,000 each).

Combine the relentless fund-raising with an increasingly shallow Hollywood-style management of public relations, and a governor who once seemed so politically adept looks out of touch with what he likes to call “the people”. He even faces a revolt in his own backyard. Last week, Warren Beatty went up to Oakland to tell the nurses' union: “Government is not show business. Government by show, by spin, by cosmetics, by photo ops, by fake events, by fake crowds—that's a mistake.”

There is a degree of thespian pique in this: Mr Beatty, who was heavily involved in Democratic politics whilst Mr Schwarzenegger was still shaping his deltoids on Venice Beach, sees himself as Tinseltown's political heavyweight. But for the moment Mr Beatty is plainly closer to the voters than Mr Schwarzenegger.

Many Californians want to know why a special election, costing anywhere between $45m and $80m is necessary, given that a regular one is scheduled for June next year. They also fear that Mr Schwarzenegger has pushed too far to the right. In a state where 43% of registered voters are Democrats and 34% Republican, three of his four measures read like a hardline conservative wish-list. Meanwhile, the fourth, Proposition 77, making redistricting fairer, appeals to neither party.

Hence a new question in California's politics: if Mr Schwarzenegger fails to convince the voters on November 8th, is he vulnerable the following November, when he stands for re-election? The polls show barely one in three want to keep Arnold in office, and he would lose to either of the two declared Democratic candidates, state treasurer Phil Angelides and state controller Steve Westly.

That still looks unlikely. It is hard to see the Gubernator, with his unrivalled name-recognition and ample war chest, quaking at the prospect of facing the barely known Messrs Angelides and Westly. Mr Beatty is another matter.

A political flirt who has hinted at running for just about every office in the land, Mr Beatty is still playing hard to get, telling the purring nurses that he “doesn't have to be an elected public servant to perform a public service”. A Field Poll back in June found that only 24% would support a Beatty candidature. That number would surely rise if Mr Beatty committed himself. But he like everybody else is waiting to see whether Mr Schwarzenegger recovers his political touch.

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Lexington

The times they are a changin'. Really

Sep 29th 2005
From The Economist print edition

Believe it or not, America is beginning to escape its groundhog decade

WE'RE told on good authority that history repeats itself, but this is getting ridiculous. The past week has been a giant flashback to the 1960s. On Saturday 100,000 anti-war demonstrators descended on Washington, DC, to chant peacenik slogans and listen to Joan Baez sing “Where have all the flowers gone?” The only thing missing was Abbie Hoffman trying to levitate the Pentagon. And that's not all. PBS broadcast Martin Scorsese's lengthy homage to Bob Dylan, alongside a week of tributes to “the years that shaped a generation” (including a special edition of “Antiques Roadshow”). Both the Rolling Stones and Jane Fonda have dragged their aged limbs on tour.

There have been a few attempts to update things. This time, some anti-war protesters wore T-shirts that read “make levees not war”, while Sir Michael Jagger has penned a song about the evils of neo-conservatism. But for the most part, everybody seems happiest with golden oldies.

Why are the 1960s so difficult to escape? One reason is the sheer size of the baby-boom generation. Giant arboreal slums of boomers now sit at the top of every establishment tree, not least the media. And like all ageing geezers they continue to see the world through the prism of their youths. Listen to Charles Rangel, a black congressman from New York, comparing George Bush to Bull Connor (the notorious white police boss in Birmingham, Alabama); or Jesse Jackson likening the peace protesters to the civil-rights heroine, Rosa Parks; or just about every pundit doing the “Iraq war as Vietnam quagmire” routine.

The other reason why the 1960s are so hard to shake off is that the decade split America down the middle, launching the culture wars that still haunt American politics and redefining America's two great parties. The Democrats became the party of people who regarded the 1960s as an unmitigated good (particularly feminists, blacks and social liberals) while the Republicans regarded the 1960s as an unmitigated evil (particularly white southerners and other “conservatives of the heart”).

This has made for “Groundhog Day” politics. Every election the same arguments appear about draft dodging, the permissive society and so on. Last year, while Iraq burned, American politics fixated on which Swift Boat veteran did what 40 years ago.

Is there really no escape? In fact, last year's election looks like the last hurrah for 1960s politics. John Kerry presumably thought that turning the 2004 election into a referendum on his war service in Vietnam was a slam-dunk, given that he fought heroically while Mr Bush skulked at home. But many voters were less obsessed by the Mekong Delta, and others remembered him as a war protester, not a war hero.

The future of both parties is in the hands of people who want to jettison their 1960s baggage. On the Democrat side, before Mr Kerry reintroduced Vietnam, the Clintonites had spent much of the 1990s distancing themselves from Eugene McCarthy. They demonised black radicals such as Sister

Souljah, embraced tough policies on crime and welfare, supported school uniforms and V-chips, and sent American bombers into Bosnia. In her preparation for 2008, Hillary Clinton has taken positions on military force and abortion rights that would have scandalised her younger self. Barack Obama, a possible running mate, is very different from the older black leaders. On the relative merits of liberal and conservative solutions to black poverty—spending more money versus changing the behaviour of the poor—he says: “It's not either/or. It's both/and.”

For their part, the Republicans have been trying to get beyond Richard Nixon's “southern strategy”. Mr Bush has appointed blacks to more senior positions in his administration than any previous president and lavished more attention on wooing black voters. The reason why black Democrats seized on the catastrophe in New Orleans to demonise Mr Bush is not because they really think that he is Bull Connor reincarnated, but because they worry that his strategy of creating a multicultural Republican Party might get somewhere.

The old road is rapidly ageing

More broadly, American society is beginning to make its peace with that divisive decade: it is becoming neither a pro-1960s culture nor an anti-1960s culture but a post-1960s culture. Polls show only 5% of voters objecting to the civil-rights revolution. For all the rage of the culture warriors, most Americans—particularly young ones—put a high premium on “tolerance”. At the same time, they also think that the counter-culture went too far. Very few people decry the nuclear family or urge people to tune in, turn on and drop out.

Society is in a process of repairing itself after the big dislocations of the 1960s, when rates of crime, pre-marital sex and family breakdown began to surge. (The annual number of divorces, for example, more than doubled between the mid-1960s and the mid-1970s.) The figures for teenage pregnancy and abortion are both declining. Crime is down (America now has fewer burglaries per head than Canada), and divorce is beginning to drop, particularly among the college-educated, as the children of divorced parents re-embrace the nuclear family. Most young Americans say they believe in God and love their country.

Mr Dylan remains such an iconic figure not because he embodied the 1960s but because, unlike many of his acolytes, he refused to be defined by the decade. Mr Scorsese makes great play about the way the folk protester infuriated his hard-core fans by going electric. But this was only one of the bard's changes. He distanced himself from his protest songs. He got God in a big way. And in his recent memoirs he boasts that his dream was a “nine-to-five existence, a house on a tree-lined block with a white picket fence, pink roses in the backyard.” That's where the flowers went, Joan.

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Argentina's economy

As Suez packs up, the locals dive in

Sep 29th 2005 | BUENOS AIRES
From The Economist print edition

President Kirchner's government wants new investors to sustain Argentina's recovery. But only some need apply

Get article background

LAST month, Argentina's president, Néstor Kirchner, intimated that he hoped to attract new foreign investors to his country during a visit to New York. His economy minister, Roberto Lavagna, met managers from foreign car firms, stressing the need for fresh investment to sustain a strong recovery from the country's economic collapse of 2001-2. So a decision on September 9th by Suez, a French conglomerate, to walk away from its contract to run the Buenos Aires water company could hardly come at a less opportune time. For the issue raised by Suez's dispute with the government is whether Argentina offers sufficient guarantees of the rule of law to attract new money.

Suez's problems arose from the decision of a previous government, in 2002, to convert water tariffs from dollars to devalued pesos and freeze them. Aguas Argentinas, the water company in which Suez has a controlling 46% stake, accepted that as an emergency measure, and maintained its service and workforce. But in years of talks with Mr Kirchner's officials, it could not strike a deal on new rules of the game. The government refused to raise tariffs as much as Suez wanted, or to share responsibility for some of the firm's dollar debts; new investment projects were derailed because the government insisted on the right to choose the contractors who would execute them. Suez invested $1.7 billion in Argentina; it had already written off €700m ($840m) of losses there.

Mr Kirchner wished Suez good riddance; a senior official threatened legal action if it did not serve out the remaining year of its contract. Mr Lavagna, who has often said that the government should be more flexible with privatised utilities, insisted that Suez's departure would have no effect on other potential investors. Many others are less sanguine. “Argentina will pay a cost for this,” says Daniel Artana of FIEL, an opposition-leaning Buenos Aires think-tank. Foreign investors “will see that they didn't settle a dispute.”

But Argentina's recovery has consistently confounded the naysayers. The economy is set for a third straight year of growth of over 7.5%. Luck, in the form of high prices for farm exports, has played a part. But despite Mr Kirchner's penchant for economic intervention, and his tough approach to foreign firms, investment has recovered almost to its level of the late 1990s (see chart)—a level high enough to allow the economy to grow at a steady 3.3% a year, says Mr Artana.

The problem is that faster growth is needed to help the 38.5% of Argentines who still live in poverty in a once-rich country. And luck can turn. According to Mr Lavagna, the share of investment in GDP needs to rise by two percentage points to sustain healthy growth.

Much recent investment has been in housebuilding and by small firms reinvesting profits—“too many bricks and too few machines” as Claudio Loser, an Argentine former IMF official, puts it. Larger firms remain cautious, especially about long-term projects. Several things hold them back. They include doubts about the government's intentions; an annual inflation rate which is creeping towards double figures; and the still partly unrepaired state of Argentine capital markets. In addition, continuing price controls restrain investment in energy infrastructure, raising fears of power and fuel shortages next year.

Foreigners, in particular, will need reassurance on many of these points. But does Mr Kirchner really want them? Only in some businesses, seems to be the answer. The evidence is that he would prefer utilities to be controlled by locals. Earlier this year, another French utility, Electricité de France, sold 65% of Edenor, a big electricity distributor, to Dolphin, an Argentine private equity fund, for some $100m.

Dolphin's boss, Marcelo Mindlin, is well-connected with the government, although many of his investors are foreigners. On taking over Edenor, he obliged Mr Kirchner by accepting a smallish tariff rise and dropping the company's claim against the government at the World Bank's International Centre for the Settlement of Investment Disputes (where foreign firms are demanding almost $20 billion in compensation from Argentina). In return, the government may provide Mr Mindlin with cheap loans for new investment. Officials say that after a congressional election on October 23rd they will move to settle disputes with other energy providers.

Some of Argentina's privatisations of the 1990s were flawed by corruption and monopoly, but electricity and water were successful, with tariffs falling and coverage expanding under arms-length regulation. The new model looks more like *criollo* capitalism, in which favoured businesses operate in close partnership with government. It may work, for a while at least. But foreigners, even in other businesses such as manufacturing, may want firmer guarantees before banking on it.

Economist.com WORLD LATIN AMERICA

Paraguay and the United States

Improbable allies

Sep 29th 2005 | ASUNCIÓN
From The Economist print edition

A flirtation unsettles the neighbours

LANDLOCKED in South America's sweaty heart, Paraguay achieved independence in 1811 but waited a century and a half for its first visit by a head of state from outside Latin America, Charles de Gaulle, in 1964. So it is not surprising that visiting dignitaries cause a stir. Donald Rumsfeld, the United States' defence secretary, caused more than that when he dropped by in August. The media in nearby Argentina and Brazil saw the visit as a prelude to a permanent American base in Paraguay and the country's withdrawal from Mercosur, a four-country trade block dominated by Brazil. That prompted Brazil to lay down the law. “Paraguay must understand that the choice is between Mercosur and other possible partners,” declared Celso Amorim, Brazil's foreign minister, last month.

In fact, the United States may not be planning to turn Paraguay, a country of just 6m, into a strategic appendage. But Mr Rumsfeld's 18-hour “courtesy call” was not merely that. Both countries see in each other a potential partner in managing regional worries.

For Paraguay, the main worry is Mercosur, and Brazil in particular. Although trade within Mercosur is supposed to be free, Paraguay complains that its neighbours strangle its exports in red tape. When convenient, Brazil ignores its Mercosur partners, for example by awarding China “market economy” status. Paraguay recognises Taiwan. Its Mercosur partners “proclaim integration but work very slowly toward achieving it,” laments Luis Alberto Castiglioni, the vice-president.

The 300,000 Brazilians who have settled in Paraguay own many of its most productive farms. But they speak Portuguese, prefer samba to local music, and their children attend Brazilian schools. One day, some Paraguayans fear, Brazil's flag will follow its culture. “Our sovereignty is threatened by Brazil, not by the United States,” says Carlos Mateo Balmelli, a senator from the opposition Liberals.

To the United States, Paraguay looks like a friend in a troubling region. It sits at the southern end of an arc of instability, a chain of weak democracies that are being undermined, the United States alleges, by Venezuela's leftist president, Hugo Chávez. Paraguay's democracy is also shaky and its discontents profound. But the United States regards its president, Nicanor Duarte Frutos, as a serious reformer. An American official in Asunción says he has made “good progress” in fighting illegal drugs and pirated goods and in blocking financing for terrorist groups—all of which flourish at the spot where Paraguay's border meets Brazil's and Argentina's.

It is easy to imagine the United States wanting to counter instability in the neighbourhood with a

military or intelligence presence. But Americans and Paraguayans alike scoff at claims of a base at Mariscal Estigarribia, close to the Bolivian border (the scene of a 1932-35 war). These claims caused particular alarm in Bolivia, which may soon elect an ally of Mr Chávez (see article). But, according to the United States, the only change in their low-key military relations is that Paraguay has approved several (small-scale) American exercises over the next 18 months all at once, rather than singly.

Paraguay is hoping for $35m in extra aid from the United States' “Millennium Challenge Account”, which rewards countries for fighting corruption and freeing enterprise. What Paraguay really craves is more access for its clothing, beef and organic sugar. Mr Castiglioni wants Mercosur to give Paraguay a “waiver” to negotiate trade agreements with the United States and other countries. Uruguay, another member of Mercosur, boosted exports to the United States without leaving the block. But Paraguayans are still unsure how much the United States is prepared to invest in their budding friendship.

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Bolivia

Electoral uncertainties

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From The Economist print edition

Legal fuel on a political fire

Get article background

IN JUNE, for the second time in 20 months in Bolivia, the president was toppled by weeks of protests. Calm returned only when an early election for president and Congress was fixed for December 4th. Now the Constitutional Court has put that date in doubt, in a ruling that bears on a widening regional split. Unless the politicians move fast, more turmoil could ensue.

Under the constitution, the 130 seats in the lower house of Congress are supposed to be redistributed after each national census. The latest census, in 2001, would take six seats from La Paz, the capital, and the impoverished Altiplano, and give four to Santa Cruz, an eastern boomtown. Western Bolivia is already sore at Santa Cruz's demands for autonomy. To avoid further rows, Congress decreed that the December poll would use the 1992 census. The court, rightly, struck this down as unconstitutional.

Many hope that the election produces a government with a clear mandate, breaking the deadlock between the political establishment and various radical movements who claim to speak for indigenous Bolivians. It could go the way of the radicals. A poll by Apoyo, a Peruvian firm, puts Evo Morales, a left-wing coca-workers' leader who backed the protests, in front with 28%.

Some among the middle-class are starting to think it would be less bad to have Mr Morales in government than in the streets. That is partly because Mr Morales is sounding more moderate, if not always convincingly. He wants to legalise coca, but says his government would have “zero tolerance” for cocaine traffickers. His campaign has played down previous talk of nationalising the gas industry. Meanwhile, the traditional parties have failed to unite behind a single candidate: the Apoyo poll gave 22% to Jorge Quiroga, a conservative ex-president, and 19% to Samuel Doria Medina, a cement magnate and former minister.

Eduardo Rodríguez, Bolivia's caretaker president, insists that the election will take place on schedule. His aides are talking to Congress on amending the electoral law. The electoral authority has said a decision must be made by October 8th. If Congress amends the law, it risks inflaming regional tension. But if the election is delayed, the radicals may take to the streets. Either way, Bolivia's interlude of calm may soon be over.

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Economist.com WORLD NORTH AMERICA

Canada's CBC

Use it or lose it

Sep 29th 2005 | OTTAWA
From The Economist print edition

A lockout at a controversial icon

SHORTLY before the Canadian Broadcasting Corporation (CBC) locked out 5,300 of its 9,000 employees on August 15th, Michele Sparling, the management's chief negotiator, declared: “This is the hill we will die on.” Seven weeks later, those words look ominous. Many of CBC's most familiar faces are on the picket line. Managers have had to fill the schedules with many inept stand-ins. Some in the media industry reckon that after the dispute ends, Canada's public-service broadcaster may be badly diminished or even doomed.

The lockout followed 15 months of talks on a new agreement between CBC and the Canadian Media Guild, a merger of three unions. The dispute centres on the management's desire to put more workers on temporary contracts, to give it the flexibility it says it needs to tackle multi-channel broadcasting, satellite radio and podcasting. The guild's response is that 30% of CBC's workforce are temps already, a higher percentage than at commercial rivals, and that the corporation needs a permanent creative core.

Like other public-service broadcasters, CBC faces a harsher world. Its parliamentary grant of C$950m ($800m) is in real terms C$400m less than it received before the government slashed budgets in the mid-1990s to eliminate a huge federal deficit. The corporation has contrived to generate C$470m this year from property and other income. But the staff has shrunk and some quality programmes were axed.

The guild appears to be winning the propaganda war over the dispute. It has the support of many writers to newspaper letters' pages. Management had to abandon plans to film the swearing-in of Canada's new governor-general, a former CBC employee, for fear that she would not cross a picket line on Parliament Hill.

CBC's defenders cherish it for its Canadian content and serious programmes. They see it as an essential bulwark against American culture. But how widely shared is that view? A poll by Ipsos-Reid last year found that half of respondents (and a plurality among those who vote Conservative) wanted parliament not to cut CBC'S funding. But another poll found that only 10% of respondents feel “deeply inconvenienced” by the dispute (and 27% slightly so). Political opinion is polarised. Liberals like CBC. But Conservatives see it as biased against them. Bev Oda, a Conservative MP who worked for a private broadcaster, questions whether ratings of 12% for CBC English-language radio, and less for its television, justify so much public money.

On September 26th, the labour minister invited the negotiators to his office, and declared that he had locked them in. The betting is that the dispute may end by October 5th, when ice hockey starts up after its own year-long lockout over player wage demands. Canadians found they could live without hockey. Journalists can hardly claim to be more indispensable.

Colombia

Carrying coffee to Seattle

Sep 29th 2005 | BOGOTÁ
From The Economist print edition

A new venture for a Latin American brand

Reuters

Mine's a skinny frappuccino, Juan

Get article background

MOUSTACHIOED, poncho-clad and middle-aged, Juan Valdez hardly seems like the perfect vehicle to reach the world's coffee-drinking youth. But Colombia's National Federation of Coffee Growers reckons there is new life in the resolutely unhip Valdez, an idealised farmer with a mule called Conchita who since the 1960s has been the public face of Colombian coffee. To prove the point, it has launched Valdez into a joust with the likes of Starbucks.

Since 2002, the federation has opened a dozen coffee shops in Colombia under the Valdez name. Over the past year, it has opened stores in New York, in Washington, DC and, boldly, in Seattle, the home town of Starbucks. Some 300 more shops are planned for Europe, the Americas and perhaps Asia over the next five years.

The coffee shops represent a belated effort by the Colombian coffee federation to grab a slice of the world market for speciality coffee. Set up in 1927, it acts as buyer, marketer, technical adviser and banker to Colombia's 560,000 coffee farmers. For 60 years, it formed the backbone of the country's economy. But in recent years, a world coffee glut has brought hard times for the federation and its farmer members.

The coffee-shop market is crowded in many countries; in the United States, Starbucks has 51% of the market. But the federation reckons it can carve out a profitable niche. It is exploring the purchase of small and medium-sized chains of existing coffee shops in the United States, with the aim of converting them into Juan Valdez franchises. The stores, which have airy interiors of Colombian wood, emphasise the quality of their coffee rather than trying to rival Starbucks as a social spot, according to Gabriel Silva, the federation's boss. And Juan Valdez is one of Latin America's few successful brands: he is known to 50% of American consumers, according to Interpublic, an advertising agency.

The stores in Colombia are profitable. To finance the push abroad, the federation talks of getting its members to subscribe to a share-offering worth 20 billion pesos ($8.7m). The whole venture represents a gamble for Colombia's coffee farmers. If it works, the federation will use the profits to restore some of its spending on rural development, which it has been forced to cut. But Juan Valdez and Conchita have a long, hard ride ahead of them.

Protests in China

The cauldron boils

Sep 29th 2005 | BEIJING
From The Economist print edition

AP

A rise in mass action worries the party, prompting more intolerant measures

Get article background

THE Chinese government is getting increasingly twitchy about what officials say is a rapid growth in the number and scale of public protests. In its latest bid to quash them, this week it announced a sweeping ban on internet material that incites “illegal demonstrations”. Does China face serious instability? Probably not, for now at least. But in the longer term there are reasons to worry.

Quashing unrest has ever been a priority for the Communist Party. But over the past year or so it has put even more emphasis on tackling “mass incidents” as it calls the protests. These include a wide range of activity, from quiet sit-ins by a handful of people to all-in riots involving thousands. Almost always, they are sparked by local grievances, rather than antipathy to the party's rule. Yet China's most senior police official, Zhou Yongkang, has said that “actively preventing and properly handling” mass incidents was the main task for his Ministry of Public Security this year.

According to Mr Zhou, there were some 74,000 protests last year, involving more than 3.7m people; up from 10,000 in 1994 and 58,000 in 2003. Sun Liping, a Chinese academic, has calculated that demonstrations involving more than 100 people occurred in 337 cities and 1,955 counties in the first 10 months of last year. This amounted to between 120 and 250 such protests daily in urban areas, and 90 to 160 in villages. These figures are likely to be conservative. Chinese officials often try to cover up disturbances in their areas to avoid trouble with their superiors.

Under Mr Zhou's orders, police forces around the country this year have been merging existing

anti-riot and counter-terrorist units into new “special police” tasked with responding rapidly to any mass protests that turn “highly confrontational”. Police officials say the existing units were too sluggish, too poorly trained and ill-coordinated to handle the upsurge in disturbances. The special police are to form small “assault squads” to tackle incidents involving violence or terrorism.

Only a few years ago, news of specific incidents seldom filtered out to foreign journalists. Now, thanks partly to a freer flow of information helped by the internet, by mobile telephony and, more rarely, by a slightly less constrained domestic press, hardly a week goes by without some protest coming to light. In June, thousands of people rioted in the town of Chizhou, in the eastern province of Anhui, after an altercation between a wealthy businessman and a cyclist over a minor traffic accident. In August, hundreds clashed with police in a land-related dispute that still simmers in the village of Taishi, in the southern province of Guangdong. Last month, the police in Shanghai detained dozens of people protesting against being evicted from their homes.

In some ways, this unrest makes China look a lot more like a normal developing country than the rigidly controlled system it was until the early 1990s. It is becoming increasingly common to encounter small-scale protests in Chinese cities that only a few years ago would have horrified order-obsessed cadres. An apartment block near your correspondent's home in Beijing has for weeks been scrawled with slogans protesting against the adjacent construction of a petrol station. “We want human rights,” says one. Residents say the police have not interfered, save to warn them not to protest during a big political gathering in the city.

Chinese officials often say that greater social unrest is normal in developing countries with a per capita GDP between $1,000 and $3,000. China's GDP per head surpassed $1,000 in 2003. But this appears to be little consolation. In August last year, President Hu Jintao appointed a high-level team, headed by Mr Zhou, to supervise the handling of protests and petitions. Official sources say Mr Hu dwelt on protests in a speech to party leaders in September 2004 and at the party's annual economic planning meeting in December. Late last year the party issued a document to senior officials telling them how to deal with unrest.

According to these sources, Mr Zhou's speeches are laced with warnings that political dissidents might try to manipulate local protests to put pressure on the party itself. This fear explains why the party has further squeezed non-governmental groups and dissidents in recent months. China Development Brief, a newsletter on Chinese civil society developments, reported that in recent weeks China's secret police had been interviewing staff of Chinese NGOs that receive foreign funding, as well as Chinese staff of foreign NGOs in China, about the purpose of their work. The government has suspended the registration of new international NGOs pending the outcome of these inquiries.

The party's dilemma is that much of the unrest is a product of the rapid economic growth that it is so keen to maintain. The outlook of many urban Chinese has changed profoundly since the 1990s as a result of the privatisation of hitherto heavily state-subsidised housing. Anxious to protect their new assets, property owners have increasingly clashed with developers, and their government backers, who have been trying to cash in on the resulting boom by erecting shopping malls and luxury housing. The expansion of cities has fuelled clashes with peasants whose land is needed for construction.

Some argue that these mostly isolated protests, if handled sensitively, could help China maintain overall stability by providing people with a way of venting frustrations. But Mao Shoulong, at Renmin University of China in Beijing, says the unrest is a sign that China lacks channels for people to air discontent in a more orderly fashion. Widespread corruption and an increasingly conspicuous wealth gap fuel a contempt for officialdom that can easily erupt into the kind of class-based rioting that occurred in Anhui in June.

And should the economy falter, urban China could be faced with the twin dangers of an angry middle class saddled with big mortgage commitments and declining property prices (a problem China has not yet had to face), as well as a big increase in the number of unemployed, who, along with unpaid pensioners, are the main participants in protests in those parts of the country left behind by the current boom. Widespread middle-class discontent, combined with blue-collar dissatisfaction, would be a much bigger threat to stability than China now faces.

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Economist.com WORLD ASIA

China and Hong Kong

Unfavoured guests

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From The Economist print edition

The Legislative Council visits the people's paradise

Get article background

AFP

Leung comes to the party

MORE than 16 years after the crushing of the Tiananmen Square protests, could China at last be ready to forgive its supporters? This week, for the first time since 1989, China let the entire membership of Hong Kong's Legislative Council, its quasi-parliament, visit the mainland. Among the legislators were half a dozen members of a pro-democracy organisation that China has condemned because of its support for the protest.

China's abhorrence of the Hong Kong Alliance in Support of Patriotic Democratic Movements in China has hugely complicated its relationship with the council, known as Legco. Since 1989, current and former leaders of the Alliance have been barred from making visits to mainland China. This ban has affected several Legco members.

And yet, on September 25th, Chinese officials in Guangdong province, which borders Hong Kong, courteously received 59 Legco members (one member of the 60-strong body could not make it), including Leung Kwok-hung, a hirsute maverick known as “Long Hair” whose radical pro-democracy group China loathes as much as it does the Alliance.

China's tolerance still has its limits. Mr Leung tried to meet Guangdong's party chief, Zhang Dejiang, wearing a T-shirt showing a lone protester standing in front of tanks near Tiananmen Square. At the urging of Chinese and Hong Kong officials, he donned a less provocative shirt. Legislators who raised the Tiananmen protests with Mr Zhang were given a polite brush-off. There was no promise that the democrats could visit the mainland again.

The delegation was led by Donald Tsang, who was appointed by China in June as Hong Kong's second post-colonial leader. Mr Tsang helped persuade the Chinese authorities to organise the trip as a way of mending fences with the democrats, who had been largely shunned by his predecessor, Tung Chee-hwa. Few are convinced that this signifies real change in China's dismissive attitude towards democracy in Hong Kong. But Ronny Tong, a legislator, says the discussion of Tiananmen was at least a breakthrough: “In the past they would have told us to shut up.”

Curiously, in Beijing, the Communist Party is preparing a commemoration in November of the 90th anniversary of the birth of Hu Yaobang, the relatively liberal party chief whose death in April 1989 triggered the Tiananmen protests. This may be a gesture to liberals, but it will not herald a re-evaluation of Tiananmen. Though Hong Kong legislators may raise Tiananmen behind closed doors

with Chinese officials, it is still taboo for most Chinese.

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Economist.com WORLD ASIA

Uzbekistan

A show trial

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From The Economist print edition

Survivors of a massacre face execution

Get article background

IN TRYING criminal cases, judges in Uzbekistan have a great advantage: the defendant always pleads guilty. The 15 men brought to trial before the supreme court in Tashkent, the country's capital, last week were no exception. Each pleaded guilty to charges of having led an armed Islamic insurgency in the eastern city of Andijan on May 13th that led to mass killing, and each begged for forgiveness.

But oddly, no one, with the possible exception of the Uzbek authorities, believes them. Human-rights groups have documented the liberal use of torture in Uzbekistan's prisons as a means of extracting confessions. Besides, eyewitnesses to the violence who fled to neighbouring Kirgizstan have said that the government, and not the defendants, conducted a massacre of anti-government protesters in Andijan. Calls for an independent investigation into the killings have been rejected.

The violence followed another trial, of 23 local businessmen in Andijan, who were also alleged to be Islamic extremists, a charge often levelled at the government's opponents. On the night of May 12th, a group of their supporters attacked a police station and an army garrison, stole weapons, then stormed the jail where the businessmen were being held, freeing them and other prisoners. They also seized a government building. The next day thousands of protesters, young and old, gathered in the town's main square to demand democracy and economic reforms. Hours later soldiers were ferried into the square in armoured personnel carriers, and began shooting at unarmed demonstrators, killing an estimated 700-1,000. The Uzbek government puts the death toll at 187, and says most of the dead were militants.

No one has presented any visual proof of the massacre, or a verifiable count of the dead: the bodies were quickly collected and buried in unmarked mass graves; the handful of journalists present were detained and their equipment confiscated. Yet reports of the killing sent shock waves through Central Asia. In particular, the incident exacerbated Uzbekistan's long-standing tensions with Kirgizstan, where more than 400 survivors of the killing found refuge. The Uzbek government insisted the refugees return, both by exerting pressure on Kirgizstan's government and by dispatching relatives of the survivors to persuade them to follow its bidding.

At first, Kirgizstan, which depends on Uzbekistan for natural gas, seemed to cave in to the pressure, returning four of the refugees. But in July, under pressure from western diplomats, Kirgizstan allowed the United Nations to airlift 439 refugees to Romania, whence they were dispersed among other countries. Inevitably, Uzbekistan retaliated. It ordered America, which was involved in the evacuation, to vacate its Karshi-Khanabad air base—from where it supplies its troops in Afghanistan—in the south of the country within 180 days. In the ongoing trial, one defendant has claimed that the American embassy in Tashkent financed the uprising in Andijan. Another three defendants have told the court that they had trained at military camps in Kirgizstan.

Assuming they are convicted, the defendants face execution. In total, more than 100 people may be tried for the same alleged crimes. Whether this will keep President Islam Karimov at the helm of a country still seething with anger at the atrocity is still to be seen.

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Afghanistan

Bowled over

Sep 29th 2005 | KABUL
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Amid the ruins of war, cricket flourishes

Pity the umpire

ON DUSTY patches of bomb-levelled wasteland, Kabul, Afghanistan's capital, echoes to the thwack of leather balls on willow cricket bats. Scarcely a football, Afghans' traditionally preferred orb, is to be seen. As a testament to the wars that have ruined the country, clearing space for urban cricket pitches, this is revealing: in recent years, some 3m Afghan refugees have come home from Pakistan, taking cricket, a game originally brought to the subcontinent by British invaders, into new territory.

The Afghan national cricket team was founded in 1995, after the withdrawal of the Soviet army had allowed the first wave of refugees to return home. A second wave soon followed, in the ranks of the Taliban. Raised in refugee camps in Pakistan, the Pushtun fanatics have an antipathy to bare-legged footballing that is well known. Their fondness for cricket is less so. Yet the Taliban's removal by America was a greater boost to the game, because it sent millions more cricket-playing refugees scurrying homewards, and brought the Indian-educated—and therefore cricket-mad—Hamid Karzai to power.

According to the Afghan cricket federation, the country has 360 registered clubs. Last month, it opened a cricket academy in Kabul. Next year, construction of a national cricket stadium is to start. The national team is improving: this year, at a tournament in Dubai, it beat Malaysia and Bahrain. At a competition in Nepal, the national youth team beat Brunei by a world-record margin.

Unused to success, Afghans enjoy these triumphs. One wasteland player, Mujeebullah Rahmani, beamed as he predicted that Afghanistan would soon beat England, the world's form team. Mr Karzai is also enthused: during an audience with the national team, he promised each member a Toyota off-road vehicle if they would only beat Pakistan.

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Economist.com WORLD ASIA

Indonesia

Easing the chocks

Sep 29th 2005 | JAKARTA
From The Economist print edition

Fuel prices are set to rise, but the blow is softened for the poor

Get article background

TO MUCH consternation, Indonesia's President Susilo Bambang Yudhoyono has said he will raise government-controlled fuel prices on October 1st. His aim is to cut a crippling fuel subsidy—at current prices, around $11 billion in 2005, or 5% of predicted GDP—and stabilise Indonesia's ailing currency. Indonesians currently pay about 30% of the market price for their fuel; government officials say this rise will be of at least 50%, and that by the end of 2006 prices will match the market rate.

Tinkering with fuel prices proved problematic for Mr Yudhoyono's predecessors. When one dictator, Suharto, raised them in 1998 it precipitated his downfall, while, in 2003, Megawati Sukarnoputri revoked an increase following widespread protests. But Mr Yudhoyono has so far fared better: he enforced a 29% price rise in March after promising to invest in health and education with the cash saved.

Attempting a second rise so soon is a grave political risk, in the opinion of many analysts, particularly since Mr Yudhoyono has delivered few of the benefits he promised. Many of the president's opponents believe he should clamp down on the smuggling of fuel, estimated last year to have cost the government $860m, before further burdening Indonesians. About 60 people have been arrested in the past month for alleged smuggling, but most are small fry and their detention has done little to convince the public that the problem is being seriously addressed.

As his second price-rise looms, Mr Yudhoyono has made few promises about what he will do with the extra cash it brings him. It seems certain, however, that he will introduce a compensation scheme for the 15.5m poorest households, or about 28% of the population. Modelled on similar programmes in 20 other countries, each family will receive 300,000 rupiah ($29) every three months.

Recipients were selected based on a survey measuring indicators such as the quality of their diet and housing, and given a special identity card to smooth payment. The appealing aspect of the process is that disbursements will circumvent needless bureaucracy: they will be made via the state-run Bank Rakyat Indonesia and the post office. Both these institutions participated in a similar scheme, from 1998 to 2004, to supply 3.95m poor schoolchildren and 140,000 schools with scholarships and grants after the 1997 Asian financial turmoil.

This scheme, however, is much larger and has been hastily prepared. It has not been piloted, and it has been poorly publicised among the intended beneficiaries. Further, no one will receive compensation in advance. The vast majority of people will have to wait at least ten days for their payments—a possible cause of annoyance, especially during the Muslim fasting month of Ramadan, due to start on October 4th, when tempers often fray. On the plus side, the very poorest are being overcompensated by an estimated 90%, the media generally support the idea

that fuel prices must rise, and Mr Yudhoyono's approval rating remains high.

The next few weeks could be the most delicate of Mr Yudhoyono's presidency. If the inevitable protests get out of control, he may have to back down. If not, ministers expect the compensation scheme to be the basis of a permanent social-security system, to be introduced by mid-2007 after a trial next year.

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WORLD
AFRICA & MIDDLE EAST

Syria

Lonely leader amid swirling rumours

Sep 29th 2005 | DAMASCUS
From The Economist print edition

Getty Images

Bashar Assad is in a pickle, and has no easy way out

Get article background

THE capital looks stubbornly normal. Shoppers crowd its markets in the run-up to the fasting month of Ramadan, which starts on October 4th. The biggest downtown building to go up in years, a posh hotel, is set to open soon. Opera-goers rave over a new musical, called “The Last Tale”, about a sad misanthrope who kidnaps a singer in the hope that her song will cheer him out of his gloom. But Syrians, who often complain that they are hostages to the ruling regime, know they need to do more than sing to solve the troubles of their president, Bashar Assad.

For Mr Assad, and his clan and Baath party, face a crisis as grave as any since his father, Hafez Assad, consolidated Syria's dictatorship 35 years ago. The regime has survived big dangers before, from losing wars with Israel (which still occupies Syria's Golan Heights), to a bloody insurgency by the Muslim Brotherhood that was crushed in the 1980s.

Soviet backing and pan-Arab sentiment helped then. But Syria now has no friends at all, except distant, non-Arab Iran. America, the sole superpower, has grown overtly hostile, and sits right next door in Iraq; the Bush administration accuses Syria of abetting jihadist infiltration of the Iraqi maelstrom, backing groups that America deems terrorists, meddling in Lebanon and oppressing its own people. America's ambassador in Iraq recently declared that “all options are open” regarding how Syria might be punished. Influential Arab countries such as Egypt and Saudi Arabia, which used to condemn such aggressive talk, have tired of Syria's countering bluster and now shrug indifferently.

If it were just American chest-thumping, Mr Assad might feel secure. But a new threat has rapidly emerged in Lebanon, the small neighbour that Syria is more used to seeing as a playground, strategic buffer and, some would say, colony. Last spring, the groundswell of anger after the assassination of a long-serving Lebanese prime minister, Rafik Hariri, made Syria end its decades-long troop presence, then obliged it to stand by as the Lebanese voted in a staunchly anti-Syrian government.

The humiliation did not end there. The UN sent a special prosecutor, Detlev Mehlis, to investigate the Hariri killing. The tight-lipped German recently had four Lebanese security chiefs known for their closeness to the Syrian regime arrested. Now, after much delay, Syria has submitted to his demand to question their Syrian counterparts. That means not just those responsible for intelligence in Lebanon, but also their bosses in Damascus, including, some say, Mr Assad's brother, Maher, who commands the Republican Guard, and their brother-in-law, Asef Shawkat, Syria's overall intelligence chief.

Mr Mehlis is not due to issue his findings until October 25th, and has said that he has no Syrian suspects. Yet his presence at a heavily secured resort near Damascus has caused much trepidation. Many Syrians assume he will finger top regime figures; the main question is how high in the hierarchy, and how close to the Assad family, the accusations will reach. Whatever it does turn up, Mr Mehlis's investigation, backed by the clout of the UN Security Council, will deeply embarrass Syria's government. Should there be proof of complicity or worse, and should Syria fail to hand over suspects for trial, Mr Assad's government is sure to be punished by further isolation, and an internationalisation of sanctions that are now unilaterally imposed by America.

Strains, not surprisingly, are showing at home. Internal opposition groups are small, fractious and closely watched. But general resentment runs high, against such ills as corruption, unemployment, sky-high house prices and the privileged place of Mr Assad's Alawite sect, which makes up 15% of Syria's mostly Sunni Muslim population. Sporadic unrest in the provinces has pitted restless Kurds, Ismailis and Druze against police or against other sects.

Sunni extremists, who once refrained from attacks in Syria in recognition of its support for Iraq's “resistance”, may have changed tactics. Gun battles between such groups and police now break out regularly. Businessmen, many of them Sunnis, complain they are tired of uncertainty. Cash is said to be flowing rapidly abroad. At least one senior ousted member of the regime, a Sunni, is said to be living in a plush hotel in Paris owned by the Hariris: that cannot bring much comfort to former colleagues.

When Syria withdrew from Lebanon, Mr Assad tempered his embarrassment by promising to speed reforms. Little has changed. The Baath party said it would revise laws that hinder the emergence of rival political parties, but has taken no measures to do so. The appointment of Abdullah Dardari, a respected non-Baathist, as deputy prime minister with a mandate to open up Syria's stymied socialist economy, was heralded as a breakthrough. But Mr Dardari's good intentions have mostly been thwarted. Despite considerable public sympathy for Mr Assad, more and more Syrians now reckon that his regime may not be capable of reform.

Intellectuals in Damascus contemplate three scenarios. One would see the regime reaching a deal with America and the UN investigators, whereby some figureheads, such as Syria's main intelligence chiefs in Lebanon, including their commander, General Rostom Ghazale, would be sacrificed for trial, and Syria would comply fully with America's other demands.

There are some signs of this. One observer detects the start of a “dance of the seven veils”, with Syria grudgingly relinquishing positions long declared sacrosanct. It has tightened controls along the Iraqi frontier, and told Damascus-based armed Palestinian groups to lie low and back Mahmoud Abbas's peace-inclined Palestinian leadership. In this scenario, Hizbullah, Lebanon's

Iran-backed Shia militia, may be the next offering. Syria's support has so far insulated it from pressure to disarm, as required by the UN Security Council. Should Mr Assad decide to appease the Americans, his regime might, in the words of another Damascus observer, “lose some limbs but still be ambulatory.”

Scratches and bites, both lethal

But the other two scenarios offer Mr Assad a less rosy outlook. One is what a dissident describes as “the cornered cat”: the regime chooses to lash out at its tormentors. This could well lead to its rapid demise. Who might the inheritors be? It is hard to tell whether various Islamist groups, such as the Muslim Brotherhood, which was persecuted by Assad senior, are growing in strength. Some close watchers think its potential exaggerated; others reckon it more likely that military types may already be gaining ground inside Syria's institutions and may make a lunge for power.

The last scenario, perhaps more likely, is “the cornered scorpion”. Surrounded by fire, it stings itself. In other words, the regime would fall to an internal coup. Who might the beneficiaries be? Infighting among the Assad family and in-laws has been rumoured. The president might have another go at chucking out the powerful remainder of his father's old guard. Or the regime could turn against the Assad family. Or, perhaps most bloodily, young Sunni officers could turn against the minority Alawites who have held commanding posts in the army and regime. If Mr Mehlis's report does, in effect, mean that Mr Assad is told to sack some of his closest and most powerful advisers, or even put them on trial, this last scenario would become more plausible. For the time being, the only certainty is more uncertainty.

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Israel and Palestine

Both sides could ensure that the next chance of peace is missed

Sep 29th 2005 | JERUSALEM AND RAMALLAH
From The Economist print edition

Israelis and Palestinians are both struggling to shed their more extreme factions

AP

The bulldozer gets through once again

TWO doomsdays have, for now, been postponed. The threat of a return to an all-out *intifada* by Palestinian militant factions, after the heaviest fighting seen this year between them and the Israeli army, was averted when both the Hamas and Islamic Jihad factions said they would return to a ceasefire brokered in March. And the threat of a split in Israel's Likud party was deferred after the party's central committee voted narrowly not to bring forward the leadership primaries that will pit Ariel Sharon, the prime minister, against his main rival, Binyamin Netanyahu.

Both events showed a triumph of reason over instinct. The trigger for the violence was an explosion at a Hamas rally in the Gaza strip on September 23rd that killed 21 people. A mishandled Hamas rocket, said both Israel and the Palestinian Authority (PA), which obliquely called it a “work accident”. An Israeli missile attack, insisted Hamas, which then launched 40-odd rockets into Israel. “That was an attempt to divert attention from their own blunder, because they feared a negative public reaction,” says Khalil Shikaki, a pollster in Ramallah, the Palestinians' capital. But Israel, as it had promised to do if attacked after its withdrawal of settlers and troops from Gaza, hit back with renewed force: over a dozen air strikes. They had the intended shock-and-awe effect: the Gaza militants backed down and called for a return to the ceasefire, fearing an even worse public reaction if the Israeli bombings continued. Yet Israel is not relenting: it launched more air strikes on the night of the 27th and began to use artillery too.

The militants miscalculated, says Mr Shikaki, since they failed to account for the forthcoming Likud vote. Mr Sharon had no choice but to respond to Hamas with an iron fist. He had been heavily criticised in the party for the Gaza disengagement. The success of its aftermath—violence or calm—may decide his chances of fending off Mr Netanyahu, who is courting the disengagement's many critics.

Could Hamas's blunder have done Mr Sharon a favour, letting him display his toughness, so swinging the vote his way? Maybe. Or maybe the Likud hierarchs simply took a deep breath and realised that a possible split (Mr Sharon might try to form his own party) and an almost certain early election were heavy prices to pay for the chance of taking revenge on the prime minister. Either way, opinion polls after the committee's vote showed Mr Sharon's popularity surging among Likud members. One poll in *Haaretz* put Mr Sharon almost 14 percentage points ahead of Mr Netanyahu, after trailing six points behind him three weeks earlier.

But even if the violence dies down, the political battles are just beginning. The Likud primaries will

now be held some time between June and November 2006. Mr Sharon's victory in those is far from assured: a lot can happen before then, and loyalties may switch many times. More worrying, though, has been Israel's other, less violent, response to the Hamas rockets: the arrest of over 400 Hamas and Islamic Jihad activists in the West Bank. Many of the Hamas men picked up were likely candidates for the local elections due in December. In some places virtually the entire Hamas electoral list has been nabbed.

That seems in line with Mr Sharon's promise earlier this month that Israel would do all it could to disrupt the Palestinian legislative elections due in January if Hamas took part. It is expected to do well. Mr Shikaki's surveys give it 30-35% of the seats, and 45% to the PA's ruling Fatah party. But rather than weaken the Islamists, Israel's action could strengthen them by building sympathy among Palestinians. “Now people who might have voted for some Hamas candidates will vote for the entire Hamas list in prison,” says a senior Palestinian official.

That would make it harder to achieve what Israel has been pushing for all along: the disarmament of Hamas and other militants by the PA's security forces. Mahmoud Abbas, the Palestinian president, last week announced a small but perhaps significant first step towards that: an agreement that militant groups would no longer parade with their weapons on the streets. (The unfortunate Hamas procession in Gaza was meant to be a last shout before that agreement came into effect.)

At a peace rally this week in Ramallah, Mr Abbas pointedly sat beside Yasser Abed Rabbo, a former PA minister and a co-author of the Geneva Initiative, a plan agreed upon two years ago by peace-minded Israelis and Palestinians without the power to implement it. There was not a single masked gunman or factional flag in sight. But the narrower Fatah's margin over Hamas in the January elections, the harder it will be for Mr Abbas to continue to seek peace. “Sharon and Hamas”, the senior Palestinian concludes, “are helping each other in the most splendid way.”

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Sudan

Enemies everywhere

Sep 29th 2005 | HAMESHKOREIB
From The Economist print edition

Discord in eastern Sudan threatens the peace accord with the south

Get article background

“WE'VE learnt the lessons of Darfur,” says Sheikh Ali, who runs the town of Hameshkoreib, in eastern Sudan, for the rebel Eastern Front. “This government only listens to people who carry guns.” What he means is that, while Sudan's main southern rebel movement has, after some 30 years of on-off fighting, won a deal that promises autonomy and perhaps even eventual independence for the south, other disaffected regions must now fight for similar concessions. While strife in Sudan's western province of Darfur continues, a growing rebellion in the east is further weakening the central government in Khartoum—and could even cause the delicate north-south deal to unravel.

As the main southern group, the Sudan People's Liberation Movement (SPLM), withdraws its forces from the country's eastern belt as part of its agreement signed earlier this year with the government in Khartoum, eastern rebels are replacing them. The Eastern Front's bases are over the border, in Eritrea. Sudanese government forces and tribal militias are limbering up for a showdown on the Sudanese side of the border. There are growing fears that the government in Khartoum is planning to unleash the militias, just as they did in the west, when mounted Arab levies known as the *janjaweed* were allowed, and probably encouraged, to commit an array of atrocities against the disaffected Darfuris, leaving perhaps 180,000 dead.

The Eastern Front was set up last year as an alliance between two eastern tribal rebel groups, the Rashaida tribe's Free Lions and the Beja Congress. They were later joined by the Darfuris' Justice and Equality Movement (JEM). The rebels' gravest threat is to block the flow of oil, which is exported through Port Sudan at a rate of 300,000 barrels a day. The government also plans to build a second refinery nearby that would double the output of Sudan's refined oil within three years. That plan, too, could be stymied.

The government is rattled. A senior intelligence official privately admits that it already has three times more troops in the east than in embattled Darfur. It is vital, he adds, that government forces retake the eastern areas from which the SPLM has withdrawn.

Tension began rising earlier this year when at least 17 rioting Beja people were killed by police in Port Sudan. Since then, a steady trickle of angry young Beja men has flowed towards rebel camps across the border in Eritrea. “You can't breathe,” says Ahmed, a recent arrival in one of the

camps, who accuses the government of stealing the area's wealth while “keeping one foot on our throat...I'd rather die fighting.” The Eritrean government in Asmara is plainly abetting the Sudanese rebels, just as the Islamist government in Khartoum gives succour to the Islamist opposition in Eritrea.

For the JEM, whose heartland is Darfur, its alliance with the Eastern Front and the relocation of some JEM troops from west to east is a chance to pose as a movement with national ambitions. At present, its western branch has a representative at the on-off peace talks in the Nigerian capital, Abuja, but its eastern one does not.

The JEM's eastern commander, Abdulaziz Osher, who is based in Asmara, says that the historic peace accord between north and south is “flawed”—because it leaves his lot out of the equation; in particular, the eastern provinces are denied what he considers to be a fair cut of Sudan's oil wealth, which will be allocated in a complex formula between north and south. “The international community is again making the mistake it made in Darfur by insisting on its application and continuing to ignore those of us, whether in the east or the west, who say we're not happy,” he says.

Riots followed the death in a (probably accidental) helicopter crash in Uganda two months ago of John Garang, the southern rebel leader who had just become Sudan's vice-president in the north-south deal that provides, among other things, for a referendum in six years on full independence for the south. Since then the southerners have been fairly quiescent. But they are particularly annoyed that, in a carve-up of ministerial posts announced last month, their new leader, Salva Kiir, agreed to let the northerners keep the energy (ie, oil) and mineral portfolio as well as the finance ministry and 14 other posts, to the SPLM's nine.

The strife in Darfur is by no means over. Peace in the south is fragile. And now, to make matters worse, the easterners are demanding a bigger slice of the cake, both in budget revenue and government posts—and say they will fight to get it. Sudan is barely holding together.

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Somaliland

Trying to behave like a proper state

Sep 29th 2005 | NAIROBI
From The Economist print edition

Breakaway Somaliland has impressed the Americans by hitting al-Qaeda

THE breakaway northern bit of Somalia, Somaliland, struck a blow for full independence last week by busting an al-Qaeda cell. Embracing perhaps 3.5m of Somalia's 11m or so people, the former British Somaliland has long been a lot more secure than the country's anarchic, formerly Italian, south. If multi-party elections due this week in Somaliland are reasonably fair and open, the outside world, including the African Union and the United Nations, may have to start seriously reconsidering its status, which has been fudged since the collapse of unitary Somalia in 1991. All three of Somaliland's parties contesting the election are adamant about wanting outright independence.

A shoot-out on September 23rd in Hargeisa, Somaliland's capital, resulted in the arrest of seven men loyal to the al-Qaeda brand. Somaliland's president, Dahir Riyale Kahnin, said the men were mostly locals, trained at a camp outside Mogadishu, the still-chaotic capital of Somalia proper. Some had received training in Afghanistan; at least one was internationally known. Their aim, he said, was to destabilise Somaliland by killing leaders and foreign aid workers, four of whom have been murdered by Islamist radicals since 2003.

There was a heady whiff of convenience about the arrests. What better, the week before an election in such a fervently patriotic fief, than to demonstrate a threat to Somaliland? Some in Somalia's fragile transitional federal government, which still lays claim to Somaliland, privately say the raid was contrived. They are probably wrong. The timing may have owed something to

Somaliland politics, where voters are softened up with gifts of narcotic qat leaves, and people's votes are divided along clan lines. But western worries about al-Qaeda's penetration into the Horn of Africa are nonetheless genuine.

Perfect for Osama?

American counter-terrorism work, mostly in collaboration with local militias and the Ethiopian secret service, has gone some way to identifying extreme Islamists inside Somalia. Catching them is harder. A few operational figures are thought to be hiding in and around lawless Mogadishu, which is mostly off-limits to diplomats, UN types and aid-workers. Though a transitional government for the whole of Somalia was set up last year in Kenya, it has failed to establish an effective presence in any part of the country, and has already broken into factions. One lot has been trying in vain to run the show from Jowhar, north of Mogadishu. To complicate matters further between north and south, a self-proclaimed breakaway government of Puntland, with its capital at Bossaso, has been demanding autonomy within a federal Somalia. And the Puntlanders claim bits of eastern Somaliland.

Some of the Islamists scattered around Somalia's various parts have roots in the Egyptian bit of Islamic Jihad, others are closer to al-Qaeda. Those caught in Hargeisa may have been connected to al-Itihaad al-Islami, a group that wants to create an emirate of Somalia along the lines of Saudi Arabia's austere Wahhabi sect. They sound particularly hostile to Ethiopia, with which Somaliland's fledgling government has been cultivating friendlier relations. In July, the Ethiopians agreed to ship some of their goods through the Somaliland port of Berbera, on a road improved with European Union funds.

Even if magnified for political effect, the arrests are a powerful signal to Islamist radicals that Somaliland is no longer a completely safe haven for them—a fact underlined by the expulsion of some foreign mullahs after the raid. That is especially notable since the Saudi government's own crackdown on radical preachers means that more of them had been looking to Somaliland as a handy refuge.

The efficiency of the locally organised swoop and the steady march of democracy in breakaway Somaliland have impressed the Americans, who have a regional military hub next door in less democratic Djibouti. Expect them to give a puff to Somaliland's chances of attaining statehood proper.

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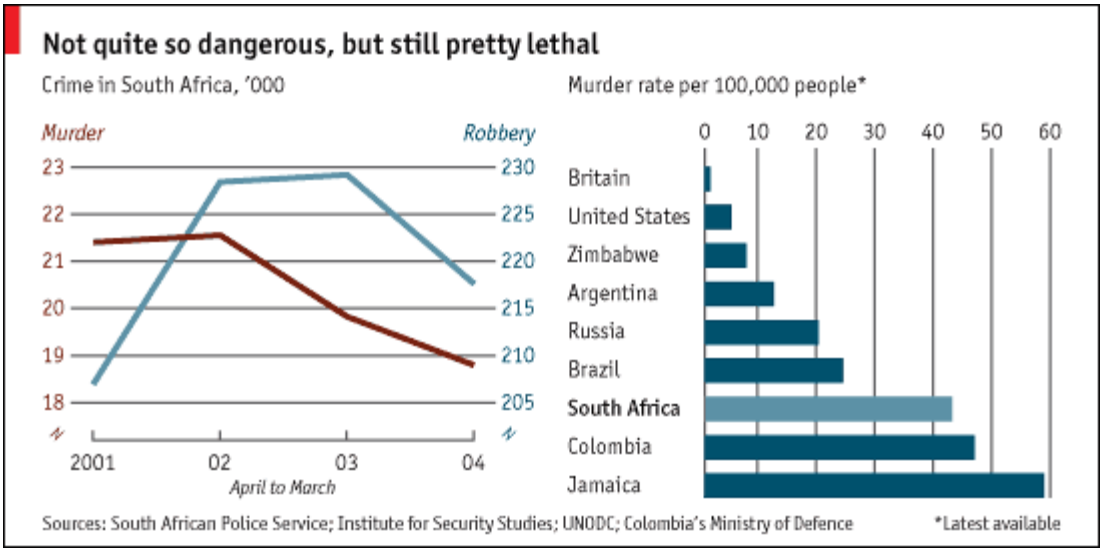
South Africa

Less crime, more fear

Sep 29th 2005 | JOHANNESBURG
From The Economist print edition

Though crime is going down, most South Africans don't feel it



Get article background

THE annual release of South Africa's police statistics has brought good news: the number of reported crimes, in most categories, is down. Fewer people were killed last year than a decade ago, the murder rate has dropped by over 12% in the past four years, carjacking has dipped by a fifth in the same period, and some 23,000 fewer houses were burgled last year than the one before. Victim surveys, which take account of unreported incidents, confirm this hopeful trend.

The police deserve some of the credit. The force now numbers 150,000, up from 100,000 four years ago. Law enforcement has improved, and the most crime-ridden areas are getting special attention. The police are also cracking down on guns: 68,000 were destroyed last year.

Yet most South Africans think crime is still on the rise. According to Anthony Altbeker, a researcher at South Africa's Institute for Security Studies, fear of crime is higher in mixed societies than in homogeneous ones. Social change and consciousness of differences bring fear, especially for minorities. South Africans of Indian descent, followed by whites, are most fearful of crime. And even though the number of crimes may get a bit smaller every year, the stock of people who have never been pick-pocketed or had a gun pointed at their face is still falling. Compared with most of the rich world, South Africa is still very violent and criminal.

Some 19,000 murders were reported in South Africa last year—about nine times the American rate and 27 times the British one. Some 55,000 rapes were reported, one of the highest rates in the world, though the authorities argue that the apparent increase in the number of sex crimes is

partly due to a greater readiness to report them. Special courts have been set up to try sex offences, and the police are now better kitted out to deal with them.

One persistent headache is overcrowding in prisons. Despite the early release of 30,000 prisoners in June and July, 150,000 people are still in jails meant for 114,000.

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Turkey and Europe

Too soon for Turkish delight

Sep 29th 2005 | ANKARA
From The Economist print edition

Corbis

Within Turkey and outside it, there are questions about the country's readiness for Europe—but also encouraging signs

Get article background

BARRING last-minute upsets, never to be ruled out as the diplomats continued haggling this week, Turkey is on the brink of realising its fondest national dream: on October 3rd, formal talks will begin on Turkish membership of a European Union at whose gate it has been waiting for 40 years.

But as so often happens, the settlement of one question—should Turkey step all the way into the EU's ante-room?—has quickly given rise to a host of others. People are already asking how long rapprochement with the EU can be sustained, in the face of opposition in Europe to Turkey—and in Turkey to Europe.

Scepticism over the Turks surfaced again this week in the European Parliament. The legislators, while endorsing the start of talks with the government in Ankara, balked at ratifying Turkey's inclusion in a customs protocol—on grounds that the ships and aircraft of Cyprus, an EU member, are still barred from Turkish ports.

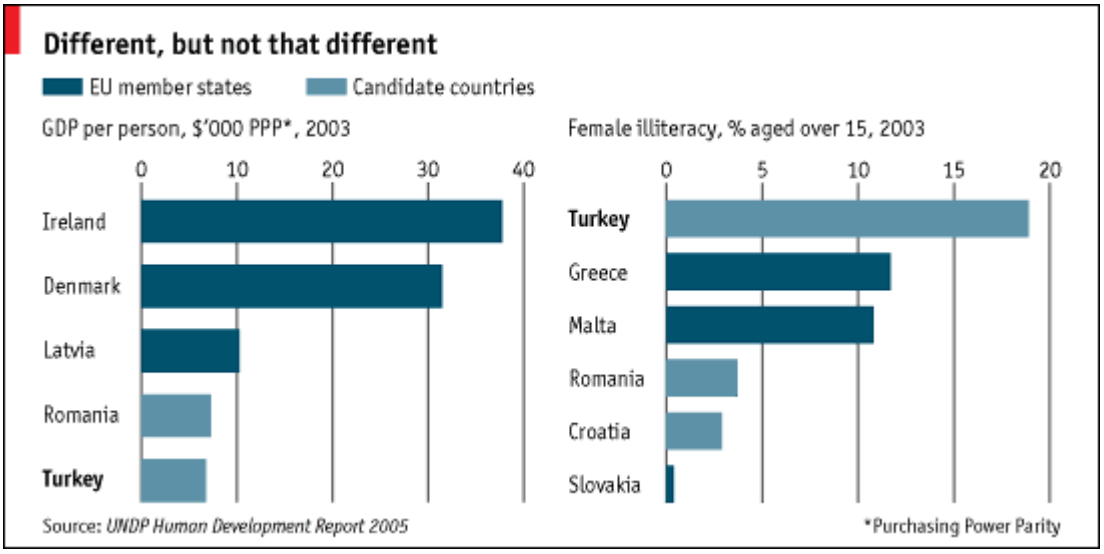
But the other part of Turkey's Euro-question is even harder: how much resistance will there be among the Turks to the changes—legal, economic, and above all cultural—that the EU is demanding?

For Turks who want a European future, there was a dollop of hope last weekend, when brave

historians managed to hold a conference in Istanbul to discuss the fate of the Ottoman Armenians. It was the first time Turkish pundits were permitted to challenge publicly the official line, holding that the mass deportation of Armenians in 1915 did not amount to a conspiracy to kill them. As participants read out letters between the “Young Turks” then ruling the empire, a rapt audience was left with no doubt that hundreds of thousands of Armenians were deliberately slain.

Planned originally for May, the Armenian forum was called off then at the behest of Cemil Cicek, the justice minister. It was nearly scuppered anew last week, when an Istanbul court used a technicality to order its cancellation. This time Mr Cicek offered a way out—changing the venue. And Recep Tayyip Erdogan, the prime minister, condemned the court ruling: the first time an elected leader had so publicly rebuked Turkey's courts.

It was also the first time that Mr Erdogan had so clearly given a lead to public opinion instead of pandering to populism. The establishment media fell in behind him, decrying the noisy nationalists who pelted the conference delegates with eggs.



Cynics, who recall Mr Erdogan's earlier moves to appease conservatives by criminalising adultery, see his recent outburst of liberalism as a last-ditch effort to clinch the October 3rd date. Be that as it may, people close to the prime minister insist he has pinned his political fortunes on further reforms, with or without the EU. “He can't compete on nationalism with the ultra-nationalists, so it's in his interest to keep on reforming,” said a western diplomat.

This may explain some other recent moves by Mr Erdogan: he dared to admit, in a speech in the Kurdish stronghold of Diyarbakir, that Turkey had erred in its dealings with the Kurds. These frank words enraged nationalists, including some members of his own party. In the country as a whole, nationalism has been bubbling: it has been rising since June 2004, when the outlawed Kurdistan Worker's Party (PKK) ended a five-year truce.

Chauvinism has surfaced in ugly ways. There have been attempted lynchings of Kurdish civilians outside their native south-east region. A recent poll shows the jingoistic Nationalist Action Party, which failed to enter parliament in the 2002 elections, would gain seats today.

As well as countering this dark mood, Mr Erdogan must cope with foes in the army who fear that rapprochement with Europe will reduce their power—and who see in Turkey's internal conflicts a chance to restore that influence. But Mr Erdogan has rebuffed army demands to re-introduce a draconian anti-terror law. Solving the Kurdish problem requires more democracy, not repression,

he insists. He may have to take further risks—for example by endorsing, despite army opposition, a deal that would coax 5,000 PKK fighters from their mountain strongholds, both in northern Iraq and within Turkey.

The coming year will be a big test of Mr Erdogan's leadership. Austria, a sceptic on Turkish entry, takes over the presidency of the EU in January. The Austrians will doubtless promote their idea of a “privileged partnership” between Turkey and Europe, instead of full membership. Next year will also see the retirement of General Hilmi Ozkok, a liberal chief of the general staff. His likely successor is the land-forces commander, Yasar Buyukanit, a more old-fashioned type of soldier. It is to keep such secularist hawks at bay that Mr Erdogan has ignored some demands from his pious voters, such as boosting religious education and easing curbs on the headscarf.

Another challenge, in his dealings both with sceptical Europeans and his own voters, is to honour his claim to be giving Turkey its first clean government. Charges of irregularity in the sale of shares in the state refinery, Tupras—and also in a tender for the operation of Istanbul's Galata port—have weakened that claim. Unless he deals with sleaze, Mr Erdogan may lose the trust of his own citizens and his European partners. That would be a pity, when the prime minister has risked so much for Turkey's European future.

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French politics

De Villepin, le marocain

Sep 29th 2005 | PARIS AND RABAT
From The Economist print edition

A prime minister's North African roots dovetail with France's keenest concerns

Get article background

AP

A spring in his step

IT TURNED out to be a symbolic visit, in more ways than one. For his first scheduled trip outside Europe as France's prime minister, Dominique de Villepin chose to fly this week to Morocco—the land of his birth, and a favourite backyard of President Jacques Chirac. Designed at least in part to discuss counter-terrorism, the trip took place as nine North Africans were arrested in France, suspected of planning attacks on the Paris transport system and on an intelligence-agency headquarters.

To the delight of his hosts in Rabat, the Moroccan capital, Mr de Villepin talked publicly of returning to his roots in “this land that I love”. In private, he described how, growing up abroad in Rabat and then Venezuela, his relationship with France was marked by a feeling of “absence and lack”, and was hence perhaps more passionate than that of other Frenchmen. His conception of France, and of its role in the world, is steeped in the imagined ideal he had of the country before he knew it.

His unapologetic talk about national destiny and national pride may sound comical to non-French ears, but in some ways it responds to the country's morose mood. “There's a search for someone who can represent France well and restore its self-esteem,” argues Dominique Reynié, a political scientist at Sciences-Po in Paris. Though the French want concrete results, particularly jobs, and find his more florid oratory a turn-off, Mr de Villepin's popularity has grown in pace with his increasingly presidential manner, especially when representing France abroad.

This was on display in Morocco, only days after the prime minister, an undeclared presidential hopeful, had stood in for a convalescing President Chirac at the UN summit of world leaders in New York. Officially, the Moroccan visit was just a regular bilateral meeting and Mr de Villepin, who served as Mr Chirac's chief of staff for many years, is careful not to appear to upstage his mentor. But, as he stepped out of his plane to review the royal guard in their snow-white uniforms and later flew off to Oujda for a special audience with King Mohammed VI, he looked like someone who had been practising for the job all his life.

Behind the discussion of social and economic development, which officially dominated the Moroccan talks, is a belief that raising standards of living is also a way to combat Islamic extremism, alongside shorter-term security measures. “We can't be too explicit publicly about counter-terrorism,” says one French official, “in order not to offend our hosts.”

The need to tighten counter-terrorist policy was underlined by this week's arrests in France. One of those detained, Safé Bourada, had been released from prison in 2003 after already serving a sentence for terrorism. His group is said to be linked to the Groupe Salafiste pour la Prédication et le Combat (GSPC), an Algerian network whose contacts with al-Qaeda have worried French intelligence officials for some time. Although there was no direct Moroccan link to the arrests, there is a broader concern about the connection between North African terror cells and al-Qaeda. Many of the suspects arrested in the wake of the Madrid bombing are Moroccan. The Moroccan city of Casablanca was itself a recent terror target.

In an apparent attempt to upstage Mr de Villepin, his chief rival on the right for the presidency, Nicolas Sarkozy, the interior minister, took advantage of the prime minister's absence in Morocco to expound his own views on terrorism. In a two-hour television programme, he confirmed his plan to unveil shortly a new counter-terrorism bill, describing the terror threat to France as “very high”. The French are keenly aware that their opposition to the war in Iraq guarantees them no protection. Their support for the anti-Islamist Algerian government, not to mention the headscarf ban in state schools or their collaboration with America in Afghanistan, provides sufficient pretext for an attack. In a recent GSPC communiqué, currently in French intelligence hands and leaked by *Le Figaro,* the group declared that, “France is our number one enemy” and “the only way to discipline France is *jihad* and martyrdom for Islam”.

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Italian politics

Ways to stop squabbling

Sep 29th 2005 | ROME
From The Economist print edition

Italy takes a wobbly step towards two-party politics

MOST Italians would prefer to have a two-party democracy. What they have instead are loose alliances of left and right, made up of nine and six parties respectively. Few people in Italy keep their opinions to themselves, so the authority of the alliance leaders is always undermined by sniping from fellow party bosses. So how, as head of an alliance, can you pull rank and make your partners pipe down for long enough to fight an election?

The question has taxed both Italy's prime minister, Silvio Berlusconi, and its opposition leader, Romano Prodi. Now, it seems, there is a solution: American-style primaries. Mr Prodi, who first backed the idea, is touring Italy in a big yellow truck to rally votes in a nationwide preliminary ballot, due on October 16th. Organisers say more than a million people will vote.

While Mr Berlusconi is less keen, the leaders of three of the four largest parties in his coalition want a vote on who will be the right's prime-ministerial candidate at the election to be held by next spring. Mr Berlusconi no longer rules this out.

Mr Prodi likes primaries more than Mr Berlusconi because he is more confident of winning. He has the backing of both the biggest groups in his coalition. But he faces a real threat from the leader of Italy's communists, Fausto Bertinotti; he has extended his old working-class power base to include young urban radicals and minority groups, such as gays. There is every chance Mr Bertinotti's more ideologically motivated followers will turn out in proportionately greater numbers to boost their man: that is what happened last time the left experimented with primaries, before the regional elections in spring, when a gay Marxist won the candidacy in conservative Puglia, Italy's “heel”.

Mr Berlusconi's problems are more serious. His coalition is trailing by up to 9.5 percentage points in the polls and its third-biggest party, the Union of Christian Democrats (UDC), has been insisting the problem is one of leadership. In the other parties, too, there is a feeling that the prime minister, who turned 69 this week, might not be the right person to stand for another five-year term.

A poll by the Ekma research institute found Mr Berlusconi would beat the UDC's best hope, the speaker of the Senate, Pier Ferdinando Casini. But he would be vulnerable to Gianfranco Fini, the foreign minister, who is also deputy prime minister and leader of the second-biggest party on the right, the formerly neo-fascist National Alliance. Mr Fini says he will not stand in a primary; his aides say he will.

Primary elections unquestionably offer a way of calming the perennially troubled waters of Italian politics. But until Italy has a system of registered party voters, they will remain a curious venture.

In the left's vote, anyone claiming to support the opposition's broad aims will be able to cast a ballot, at a cost of one euro ($1.21) to cover the expenses of polling. Nothing stops government

supporters turning out to vote for Mr Bertinotti as a way of undermining Mr Prodi. Indeed, there have been claims that the vote in Puglia was distorted in just this way. To be effective, Italy's “primaries” need be seen as accurate tests of opinion—or they will simply lead to even more squabbles.

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Lithuania and Russia

Airy disdain

Sep 29th 2005
From The Economist print edition

An argument over a crashed plane

IN COLD-WAR days, Soviet aircraft would probe NATO airspace, checking to see how fast the capitalist enemy's fighters could shoo the intruders away. Now it is happening again. On September 15th, a Russian fighter's electronics failed and it crashed in Lithuania. The pilot and the wreck have been held there, pending a Lithuanian inquiry.

There are certainly some interesting questions. Even before the Baltic states joined NATO last year, they had acquired Baltnet, an advanced radar system that looks deep into Russia. The Russians want to know how it works and how closely it is tied to a still snazzier radar in neighbouring Finland. With a surveillance aircraft positioned overhead, Russia has been flying planes to the edge of its neighbours' airspace—and sometimes beyond.

After 11 such stunts, the Finnish government complained. In June, Russia apologised, blaming human error. But Estonia, which has also recorded multiple violations, has received no apology.

Revealingly, Russia's air-force chief, Vladimir Mikhailov, has mocked the Baltic air defences as “good for nothing” for failing to spot the latest intruder. With no warplanes of their own, the Balts rely on borrowed aircraft and pilots from other NATO countries, currently Germany. “Were they drinking beer?” scoffed General Mikhailov. Other officials are more soothing, and have offered €3,000 ($3,600) in compensation. But protest banners outside energy-poor Lithuania's Moscow embassy make a sharper point: “No pilot—no gas”.

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Economist.com WORLD EUROPE

Serbia's economic upturn

A chink of light

Sep 29th 2005 | KRAGUJEVAC, SERBIA
From The Economist print edition

Glimmers of hope in Serbia's rust-belt

IT FEELS like a time-warp. Gleaming cars of a type designed in the early 1970s roll off the line at Kragujevac's giant Zastava plant. As the workers in blue overalls sip their Turkish coffee, they gaze up at portraits of Marshal Tito, the Yugoslav leader who died in 1980. Yet they are now looking forward, not back.

Zastava is often seen as a byword for Serbia's industrial decline. And if the company has suffered, so too has the town: 40,000 of its 200,000 residents used to work for Zastava. Only now, five years after the fall of Slobodan Milosevic, the demagogue who set Serbia on its course of war, suffering and isolation, are the town and the plant showing new signs of life.

In 1989, the last full year of old Yugoslavia's life, Zastava made 180,950 cars here. When the country fell apart, it lost suppliers and markets. The international sanctions imposed by the UN hurt, and during the Kosovo war in 1999, NATO bombed parts of the plant, which also makes arms. That year, just 4,500 cars dribbled off the lines; last year, 13,300. According to the mayor, Veroljub Stevanovic, well over half the working population was unemployed until recently. Even now, all of Zastava's diverse holdings in Kragujevac employ only around 13,000 people.

But then look at the chinks of light. On September 20th, after years of wrangling, Fiat of Italy struck a deal with Zastava to make up to 16,000 cars a year. At the company's arms plant, too, things are looking up: it has a $3.8m contract with Iraq. This year, says the mayor, over 7,000 new jobs have been created in the town.

The upturn matches the trend in Serbia as a whole: GDP grew by 7.5% last year. And Miroljub Labus, the deputy prime minister, says the country has pulled in $1 billion of foreign investment this year. United States Steel and some western tobacco firms have helped to turn round local industries that had virtually collapsed. On September 27th, Microsoft opened a software centre in Belgrade. Some 7,000 new firms have registered in Serbia this year.

Serbia's rate of inflation, 17.2%, is high. But that is a side-effect of recovery, and of a banking system and retail market jerking back to life. After long privation, people are chafing to buy fridges and cars.

Yet, despite all this, most citizens say life has never been as tough as now. “Our real problem”, sighs Mr Labus, “is public perception.” People do not compare their life now to that of five years ago, but rather to that of 20 years ago, the era of communist certainty.

Next week, the European Union's foreign ministers will start a set of negotiations with Serbia that are designed to lead to a “stabilisation and association” pact, and in the end, perhaps, to membership. Given that Serbia may soon face some painful constitutional changes—including the final loss of Kosovo and the break-up of its union with Montenegro—its economic upturn is good news, both for weary Serbs and their European partners.

Economist.com WORLD EUROPE

Germany's election

Between Caesar and Chernenko

Sep 29th 2005 | BERLIN
From The Economist print edition

A broad left-right coalition is the only way out of Germany's stasis

Get article background

TWO weeks after Germany's voters spoke in ambivalent terms about their next government, you might think the political barons would be edging towards a deal. Instead, they are awaiting another verdict—from the 219,000 voters of Dresden, whose poll has been delayed until October 2nd by a candidate's death.

As many as three seats in the Bundestag, the lower house, may be decided. The Christian Democrats (CDU) are in the odd position of hoping they do not get too many votes, because under the rules they might then forfeit a seat elsewhere. Even more strangely, the politician at risk is called Cajus Julius Caesar.

It is unlikely that the by-election will allow the Social Democrats (SPD), which now have 222 seats in parliament, to pull even with the CDU and its Bavarian sister party, the Christian Social Union (CSU), which together hold 225 seats. If this happened, Gerhard Schröder's hopes of remaining chancellor would obviously rise. Yet the Dresden vote, tipped to end in a photo finish, matters. Whichever camp does best in Dresden will press its claim to lead the next government. And since all other attempts at forging a majority have failed, the vote will probably mark the start of tortuous talks between the conservatives and the SPD over the terms of a “grand coalition” of all their parties.

After a show of defiance on election night, Mr Schröder is being less inflexible. He is now promising to do his best to make a grand coalition work, hinting he would step aside if need be. Other SPD leaders are implying that, if the reward was big enough, they might sacrifice Mr Schröder. Franz Müntefering, the SPD's chairman, says his party wants “to stay in government, keep Mr Schröder as chancellor and push through as much of the SPD's election programme as possible”. Decoded, this may mean the chancellor is worth giving up—for, say, half the ministries, the speakership of parliament and an SDP-influenced government agenda.

The SPD wants to talk policy first, and then bargain over jobs—the opposite of the CDU's approach. Its candidate for the chancellorship, Angela Merkel, says there will be no serious talks until the SPD agrees that it lost the election and she must be chancellor. She also wants a “common basis of trust”: the SPD must eschew other options, such as a new election.

Though the SPD will balk at these terms, Ms Merkel looks better placed than her foe. She failed to win a majority for her reform agenda, but the CDU and CSU combined are the biggest parliamentary group. Ms Merkel may yet prevail in the same steely way that she overcame her party rivals. Much will depend on the solidity of her support within the CDU. Some blame her for squandering a big lead. But nobody wants to weaken her now. Her fiercest rivals—Christian Wulff and Roland Koch, premiers of Lower Saxony and Hesse respectively—sound loyal.

This unity makes it unlikely that the CDU would accept a deal to let Mr Schröder keep power for a year or two before yielding the chancellery. It is just possible that both Mr Schröder and Ms Merkel will go. If so, few would expect them to be replaced by the people first in line: Mr Koch and Peer Steinbrück, a former SPD premier. More likely would be the “double Chernenko” option, named after a decrepit Soviet leader: Edmund Stoiber, the veteran CSU boss, as chancellor and Mr Müntefering in some other top job.

Defining an agenda may be easier. Although the two parties diverged during the campaign, they have a history of working together. In 2003, Mr Koch and Mr Steinbruck jointly presented a proposal to slash subsidies. In 2004, Mr Stoiber and Mr Müntefering almost managed a reform of the federal system. And last spring, Mr Schröder and Ms Merkel agreed, among other things, on cutting corporation tax.

A grand coalition might also be able to tackle other problems, like the baffling tax system, high non-wage labour costs and, not least, the budget deficit. But to be truly successful, such an alliance would have to go further, for instance, by reforming Germany's “financial constitution”, a cobweb of tax-revenue equalisation and joint public spending (introduced by the first post-war grand coalition of 1966-69).

If history is any guide, a new marriage of elephants would neither disappoint nor over-perform. The first grand coalition was productive: passing emergency laws, and achieving judicial reform and Keynesian demand management. But it drove some voters towards extremism. Conditions may now be right for a better outcome: Germany's big parties know they must show some results, such as job-creation, or even more voters will turn to the smaller parties, perhaps even the extremist ones. Much will depend on the chemistry between coalition leaders. If the first grand coalition was a partial success, it was mainly because Karl Schiller, the SPD economics minister, and Franz Josef Strauss, the CSU finance minister, got on well, gaining the nickname “Plisch and Plum”, after two dogs in a famous poem.

For Germans, it comes as a relief that their leaders are heading for serious discussions, though they will hardly agree by October 18th, when parliament is due to reassemble. Just as the economy has recently perked up, so hope now flickers that politics may bring a nice surprise.

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Economist.com WORLD EUROPE

Charlemagne

Choose your poison

Sep 29th 2005
From The Economist print edition

Europe's social policies offer a heady and intoxicating mixture

HENRY VIII executed his English wives but only divorced his continental ones—so by British standards, he may count as a Europhile. A scrap of comfort, perhaps, for the European Union leaders who will, at the end of this month, be wining and dining in his palace, Hampton Court, as they meet to deliberate on “the European social model”. This summit was supposed to be the big set-piece event for the second half of 2005, while Britain holds the EU's agenda-setting presidency.

The hosts recently made a discreet presentational shift; they are calling their gathering an informal meeting on “globalisation”—apparently because they realised, just in time, how little continental politicians relish British lectures on the demerits of their social and economic arrangements. They also fear, reasonably enough, that any debate on “the social model” could slide into an unseemly pan-European round of name-calling.

Yet the original impulse was right: a debate on the European social model is worth having, not least to ascertain whether any such thing exists. From the viewpoint of Washington, DC, or Beijing, there does, of course, seem to be a single, well-defined European approach: a warm security blanket, now a bit threadbare, guaranteeing people a comfortable standard of living whether they work or not—and hence reducing the incentives to work, compared with how things are in America or China.

Inside Europe, however, the contrasts between countries and regions are as striking as the similarities. In a continent that glories in political, linguistic and gastronomic diversity, there are almost as many forms of social policy as there are national drinks. All seek to reduce income inequality and poverty; all provide protection against losing your job. But they use different policies to do this, and spend different amounts of money.

The best known brand is the continental one, favoured by the French, Germans and some of their neighbours. Their system provides generous unemployment benefits and pensions. It limits, by law, the ability of firms to fire workers. It spends a lot on income redistribution, so poverty is low and income compressed. Unions, though declining, are still strong; in Germany they have a role on management boards. This is the champagne of social policy: pleasant-tasting, a luxury, and bank-breaking.

The Mediterranean alternative, preferred in Italy, Spain and Greece, also protects workers from being fired. Indeed, job-protection laws in these countries are often stricter than they are farther north. But unemployment benefits in the Mediterranean region are modest; at least until recently, the family was the cushion against adversity, not the state. These countries also make less use of taxation to lessen inequality. While the continental system reduces poverty by about 39%—against what it would have been without redistributive taxes—the Mediterranean one does so by only 35%. Call this the grappa or ouzo variety: locals swear by it, outsiders balk at it, and too much can be fatal.

Neither of these tinctures, though, provides the social protection enjoyed by the Nordic countries and the Netherlands. Their system is like aquavit: both heart-warming and bracing. They spend the most money on poverty reduction and on intervening in labour markets to help people get jobs. But these states have a Protestant work ethic: we'll help you find a job, they say, but you must work if you can. While the dole is generous, job protection laws are quite weak. In this respect, the Nordic countries are the opposite of the Mediterranean ones: the latter focus on keeping people in work; the former offer a decent dole but put fewer curbs on firing. The fizzy Franco-Germans are “generous” in both these areas (unemployment benefits and job protection).

When the sweetest taste is bitter

And it is tempting to say the English-speaking countries (Britain and Ireland) offer neither. That would not be quite right. True, their job protection is weak compared with the continental and Mediterranean systems. And their redistributive taxes are low compared with Nordic countries (and their poverty rates higher). But the Anglophones, like the Nordics, spend a lot on job centres and the like. They offer quite generous unemployment benefit, albeit not at Nordic levels. So they are also unlike the Americans, who provide much less unemployment insurance. In short, the Anglo-Saxon model is a bit like beer: not fancy, too bitter for some, but a cheap, practical way to satisfy your needs.

Europe's debate on social welfare is often couched in terms of cold-hearted Britain and America versus warm and fuzzy continental Europe. This is a caricature—and a damaging one, since it fosters the illusion among Europeans that America is the alternative to the status quo and that “reform” is code for “abolishing our welfare state”. Of course, Europeans have to adjust to the world outside, but that can be done in part by comparing notes with neighours and learning from them.

As André Sapir, of the Free University of Brussels, points out, problems are concentrated in Mediterranean and continental countries. They are much more heavily indebted than Nordic and Anglo-Saxon ones (public debt is almost twice as high as a share of national income). They have lower rates of employment and work much less. (French and Germans work about 150 hours a year less than the Nordics and 250 hours a year less than the Anglo-Saxons.) Hostility to globalisation is greater, too.

It seems unlikely that the French and Italians are going to turn into Dutch or Swedes, either in their social philosophies or their drinking habits. But over the next few years it ought to be possible for Europe's laggards to reduce their over-reliance on hiring and firing laws (disastrous at a time of fast economic change) and to increase the rewards for getting a job. And they should be able to do this without agonising about the destruction of the European welfare state. The European model is not dead. But some of its varieties look increasingly unaffordable, and like the other kind of liquor, they are destructive of honest labour.

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Economist.com WORLD EUROPE

Gordon Brown and the economy

Juddering

Sep 29th 2005
From The Economist print edition

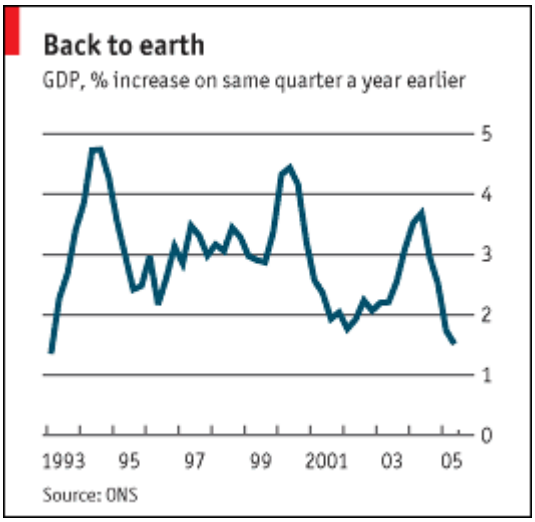
The chancellor's once solid reputation is increasingly at risk

Get article background

IF GORDON BROWN is the anointed successor to Tony Blair, then he owes it principally to his prowess as chancellor of the exchequer. Labour won the May general election by campaigning on its economic record. Tony Blair lauded his colleague as probably the most successful chancellor in 100 years. Mr Brown, who doesn't do modesty, said that he was presiding over the longest period of sustained economic growth in 300 years.

Such claims were a hostage to fortune. The worry for the chancellor is that his record will deteriorate as he waits impatiently for Mr Blair to step down. Mr Brown said in his conference speech on September 26th that he wanted to revitalise New Labour, but that lofty ambition, whatever it means, will be harder to realise if the economy starts to founder.

Already, revisions to the national accounts have shown that GDP growth since the middle of 2004 has been weaker than thought at the election. Official figures released on September 28th revealed that the economy grew by 1.5% in the year to the second quarter of 2005, the slowest for 12 years (see chart). Quarter-on-quarter, GDP growth has been below trend for the past year and manufacturing slid into recession in the first half of 2005.



With little sign of an imminent recovery, Mr Brown has had to downgrade his growth forecast for this year. In his March budget, the chancellor was able to trounce his critics by reporting that the economy had expanded by more than 3% in 2004—bang in line with his forecast a year earlier. But his hopes for a repeat performance in 2005 have been dashed. Far from growing by 3-3.5%, as Mr Brown predicted in March, the economy is likely to grow by about 2%, as he in effect admitted in America on the eve of Labour's conference.

Chancellors take credit for the good times but blame other people when things go wrong. No exception, Mr Brown has a culprit to finger. The recent oil-price shock, he says, is as big as that of the 1970s, which triggered a global recession.

The excuse is pretty lame. For one thing, the doubling of oil prices since the start of 2004 bears little resemblance to the quadrupling that occurred in the final three months of 1973. For another, the real oil price, while higher now for Americans than its peak in the early 1970s, remains lower for the British economy (see chart). Furthermore, Britain was then a big oil importer, whereas it is now self-sufficient because of North Sea production. These days the economy also uses much less

oil per unit of GDP, to such an extent that it has become the least oil-intensive among the G7 countries.

As a result an oil-price shock affects Britain less than other developed countries. According to Ray Barrell of the National Institute of Economic and Social Research, a rise in oil prices cuts GDP growth by half as much as it cuts the euro area's and by a third as much as it reduces America's. He estimates that only about a quarter of Britain's slowdown from growth of 3.2% in 2004 to projected growth of 2% in 2005 can be pinned on to higher oil prices.

The unpalatable truth is that the slowdown has been predominantly home-grown. Unfortunately for Mr Brown, it represents the payback for the long period of growth on his watch. Since he became chancellor in 1997, a surging housing market, which he acknowledged this week became a bubble, has underpinned consumer spending which in turn has sustained economic growth. Households ran down their savings and ran up debt, which has risen to a record 150% of their disposable income.

But now the housing-market boom is over. House prices rose by just 1.8% in the year to September, the lowest increase since May 1996, according to the Nationwide building society. Consumers are weighed down by the burden of servicing their debt. The mounting pressure on household budgets has taken its toll. People have rediscovered the habit of saving. The saving ratio has jumped from 4.1% of disposable income in the last quarter of 2004 to 5.0% in the second quarter of 2005.

As a result, consumers are no longer bolstering the economy. After growing by 0.9% a quarter since Labour won power in 1997, household spending has lost momentum this year. In the first three months of 2005, it increased by just 0.1%, and in the second quarter by 0.4%.

The worry for Mr Brown is that the economic weakness will persist. Over the past few years, the public sector together with consumers have been the main engines of growth. But the public-spending boom ends next April. With consumers likely to remain thrifty, this means that GDP growth will have to rely more upon business investment and exports. However, firms are likely to be cautious in making investments and exporters will have to contend with low growth in the euro area, their main customer.

A more sluggish economy will exacerbate Mr Brown's financial difficulties. Whatever his record in forecasting growth, the chancellor has been persistently over-optimistic in his budgetary predictions over the past four years. In March he said that the government would have to borrow £32 billion, equivalent to 2.6% of GDP, in 2005-06. Once again, his forecast looks too sanguine as a slowing economy and a shift to exports, which generate less tax, drive up the deficit.

Mr Brown has in many ways been a lucky chancellor. He was fortunate to have inherited from the Conservatives a healthy economy and public finances that were rapidly improving. But his luck ran out some time ago on the budget and now it appears to have done so on the economy, too. If he is now impatient to become leader, it may be because he fears what another full term at the Treasury will do to his reputation as chancellor.

The IRA's arms

Out of sight, out of mines

Sep 29th 2005 | BELFAST
From The Economist print edition

The IRA has destroyed its arsenal. Promise

EPA

Guns on the streets

Get article background

HOW can you know something has been destroyed when you don't know what it is? The answer determined the reception of the news this week that the IRA had at last put a huge quantity of guns, missiles and explosive “beyond use”.

It was hardly a straightforward operation. John de Chastelain, a retired Canadian general appointed ten years ago to clear Northern Ireland of weaponry, and his colleagues, who included a Finn, an American and a couple of priests (one Protestant, the other Catholic, naturally), logged weapons and explosives over several weeks at several dumps, then supervised the operations that disabled them.

But neither the clerics nor the experts would say what had been destroyed or how. General de Chastelain pointed to intelligence that confidently listed rifles (varying from 500 to 1,000), heavy machine-guns (20-30), Semtex (2-3 tonnes), and surface-to-air missiles.

The general said the IRA had assured him this was their entire armoury. The state of the ammunition—variously loose, in belts, or the original packaging—supported intelligence that weaponry had been gathered willy-nilly into central dumps from all over Ireland. Some could not be traced because its minders had died, some had gone to dissident groups. Nobody, the general said, could be sure if the IRA had kept any weapons back.

The uncertainty did not much bother the British, Irish and American governments, which have backed the process. They concluded that a secret army claiming the right to bear arms until

Ireland was reunited had given up its weapons without securing its goal. The gesture alone convinced them that republicans have converted to wholly political methods.

Not so the Reverend Ian Paisley, leader of the Democratic Unionist Party, who scoffed at the “falsehood of the century”. For him the lack of video, photographs and inventory rendered the exercise valueless. Mr Paisley was irked that the cleric of his choice had been passed over for a well-known liberal. He fastened on the uncertainty as proof of conspiracy to defraud unionists, insisting that the IRA had given their arms to dissidents. The threat now, he said, was from “all these other armies”.

Yet, after recent rioting by Protestant paramilitaries who have killed scores in the past ten years, Mr Paisley's scepticism sounded like a substitute for political engagement. The armies in whose weaponry Mr Paisley has shown least interest are the illegal Ulster Volunteer Force (UVF) and Ulster Defence Association (UDA). One UDA spokesman, calling the IRA move irrelevant, said loyalists would keep their guns while the Union was in danger, a favourite Paisley phrase.

An international monitoring body set up at unionist insistence to detect paramilitary activity will report on the IRA in October and January. If it finds no criminal or paramilitary activity, the governments will press the DUP to negotiate power-sharing with Sinn Fein. The only internal pressure on Mr Paisley may be his own party's ambition, and perhaps the desire at the age of 80 to hold power at last, even if it must be shared with the enemy.

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Psephology

Wooing the electorate

Sep 29th 2005
From The Economist print edition

To win power, the Tories must beat the electoral system as well as Labour

Get article background

WHEN the Tories meet in Blackpool next week for their annual conference, one thing will be on their minds: how to pick a leader who can pull off the next election. The odds on Ken Clarke—favourite with the Conservative associations—shortened, after the party rank-and-file voted on Tuesday against handing over the final choice of the next leader to MPs. But whether the victor is Mr Clarke or David Davis, the bookies' favourite, the party has a Herculean task simply to overcome Britain's electoral arithmetic.

In 1997 Labour won a general election with 43.2% of the votes cast, and gained a majority of 179 in the Commons. In 2005 Labour's share of the vote was only 35.3%, but even so it managed a majority of 66. This was the lowest share of the vote to have brought a single party to power since the partition of Ireland in 1921. Despite doing nearly as well as Labour, with 32.3% of the vote, the Tories won far fewer seats.

Labour does better out of the country's first-past-the-post electoral system thanks to a number of demographic oddities. One is that Labour constituencies are on average smaller than Tory ones. Labour is strong in Wales and Scotland, which punch above their electoral weight in Westminster, and the party does well out of long-term demographic trends, because, over time, voters tend to move out of urban (Labour-voting) areas and into suburban and rural (Tory) ones.

As a result, the average Labour-held constituency contains around 6,200 fewer voters than the average Tory-held one. Constituency boundaries are due to be redrawn before the next election to take account of such things, but this is likely to hand at most another 14 seats to the Tories. And Labour's votes go further than Tory ones because turnout is lower in Labour constituencies—so much lower that that there is an 8,500 difference in votes cast.

Some Tory MPs think that the party's salvation lies in a far more radical redrawing of constituencies. David Cameron, one of the leadership candidates, recently suggested legislating to equalise the size of all constituencies, even if that resulted in some odd geographical entities. It wouldn't make much difference. The Tories' main problem is the large number of votes they waste because their voters are inefficiently distributed: Tory MPs tend to have been elected with considerably larger majorities than Labour ones.

John Curtice, professor of politics at Strathclyde university, says a swing from Labour to the Conservatives of 1.5%, spread evenly across the whole country, would give the two parties identical shares of the vote, but, on current boundaries, leave Labour with an overall majority of 22. It would take an implausibly large swing of around 8% for the Tories to form a government. Anything in between would mean a hung Parliament. The most likely way this electoral arithmetic will change is if the two main parties win back votes from the smaller parties, whose share of the vote, at 30.6%, is at a high.

But there is one intriguing possibility. On a swing of just over 1.5%, the Tories would win the popular vote, but find themselves in opposition. Misery for the Tories, but a fillip for electoral reform.

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Civil rights

Conference kick-out

Sep 29th 2005 | BRIGHTON
From The Economist print edition

If you give people power, they will use it

HOW will Britain apply its new anti-terrorist powers? If you ask ministers, as many did during the Labour Party conference in Brighton this week, the answer comes back larded with soothing words like sensible, rational and proportionate.

But the conference showed how those dressed in a little brief authority behave in real life. An 82-year old man was bundled out of the conference hall for shouting “nonsense” during a speech on Iraq by Jack Straw, the foreign secretary. When Walter Wolfgang tried to return he was stopped by police citing the Prevention of Terrorism Act.

The burly stewards who ejected Mr Wolfgang could not have picked on a less threatening person. A Labour Party member for the past 57 years, he came to Britain in 1937 after fleeing Nazi Germany. Mr Wolfgang offered to go quietly, but the heavies wanted to make an example of him. As cabinet ministers looked on, they turfed another man out of the hall, for daring to suggest that Mr Wolfgang should be treated respectfully.

Although Britons treat abstract debate about their civil liberties as a yawn, nothing stirs them like real abuse. On the evening of Mr Wolfgang's ejection Ian McCartney, the Labour Party's chairman, issued a grudging apology. The next morning, after receiving a broadside from the newspapers, the prime minister said sorry properly.

The fuss is hardly enough to make the government tear up its anti-terrorism strategy. But it should remind lawmakers that people soon make casual use of the powers they are given, whatever the original intention.

Politicians routinely behave as if this were not so and that they should not share in the blame. While saying sorry to Mr Wolfgang, Mr Blair told the BBC that “it's not that me or anyone else has given some instruction to people to go and be heavy.” Coming just a day after he told the conference the criminal justice system should worry less about finding innocent people guilty and more about the rights of people to live in freedom and security, that rang hollow.

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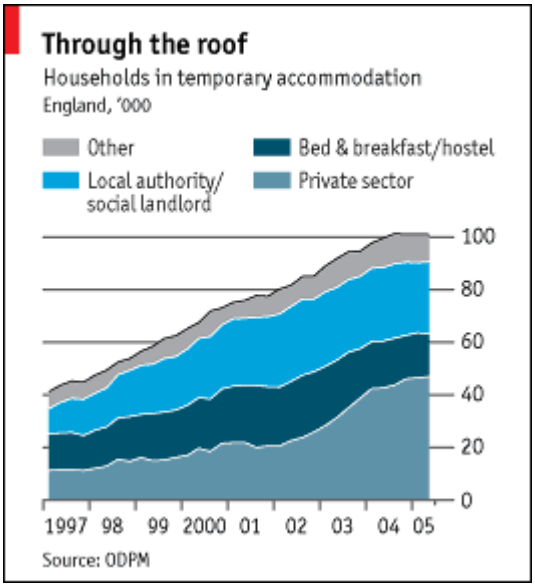
Economist.com WORLD EUROPE

Housing the poor

In limbo

Sep 29th 2005
From The Economist print edition

Britain is quietly moving towards a new way of housing the poorest



FOR a government that claims to be the scourge of poverty and social injustice, it looks like an embarrassing failure. When Labour came to power, in 1997, some 44,000 poor households were awaiting a permanent place to live. Since then, unemployment has fallen and prosperity increased, yet the number of homeless households has topped 100,000 (see chart). A blot on the record, yes, but one that conceals a more fundamental change. Britain is moving, albeit messily and reluctantly, towards a new and potentially better way of housing the needy.

Though formally homeless, few of those who lack settled abodes sleep on the streets, nor do many live in dingy hotels or hostels. Both fates are now rare, thanks to government pressure on local authorities and the homeless (rough sleepers are hassled until they agree to live under some kind of roof). Most have qualified for state housing because of poverty and vulnerability, and are housed in a variety of places while awaiting their turn.

The queue is lengthening not because there are more needy people, but because fewer cheap houses and flats are available. Under the right-to-buy scheme launched by the last Conservative government, many of the largest and best council properties have been sold to tenants at discounted rates. That allowed many to amass equity for the first time and opened a route to the middle class. But it also means a smaller safety net for the poor.

The problem is starkest in the costly London borough of Westminster, where demand so exceeds supply that it is virtually impossible to obtain social housing unless you have been certified as homeless, according to Rosemary Westbrook, the borough's housing director. Some 3,100 households in Westminster await a permanent council home—up from 1,700 in 1997-98. Waiting times are long: those who want a four-bedroom property can expect to hang around for six years. Their “temporary” accommodation is beginning to look permanent.

In the past few years, an increasing proportion have been biding their time in private housing, most of it arranged by local authorities but some leased directly from landlords. Tenants pay rent and recoup the outlay through housing benefit. That is, in some ways, an excellent solution. Private housing is both more flexible than social housing and more dispersed: pockets of deprivation like those found on council estates are less likely to emerge.

The trouble is that people who rely on housing benefit have little incentive to work, at least in the

legitimate economy. The handout is sharply tapered, meaning that it decreases rapidly for every extra pound earned. Marginal tax rates for those who receive it often touch 90%, and in areas of high rents people must earn a middle-class salary before the disincentive to working disappears.

Despite government pledges to build more of the stuff, there will never be enough social housing. The solution is to smooth the transition to the open market, and encourage those who are able to fend for themselves to move on. In encouraging private-sector provision for the poorest, Britain is taking the right course. Too bad it is penalising work.

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Universities

I've started so I'll finish

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From The Economist print edition

More students, or more graduates, but not both

Get article background

AT FIRST glance, it doesn't look that hard to become a chartered financial analyst. If you have a first degree and $2,500 to spare you can sign up to the programme run by the CFA Institute, an industry body based in America, do three exams and work for three years as an investment professional. There are no interviews, entrance exams or aptitude tests.

But there is a catch: the success rate is only 20%. Of those who sign on, 40% never show up for a single exam, while another 40% fail an exam and don't retake it successfully. This, says Bob Johnson, the programme's managing director, is a natural consequence of the combination of rigorous exams and low barriers to entry. He likens the CFA programme to an open golf tournament, which he prefers to the invitation-only kind, even though most of the extra competitors will do poorly.

Seen from this viewpoint, success rates at British universities are high: more than 77%, according to the Higher Education Statistics Agency (HESA). They are also high compared with universities in other countries. In 2000, the most recent year for which the OECD has released figures, only three of the other 20 OECD countries did better and some did far worse—Italy's dropout rate is three times as high as Britain's. The OECD is updating its research, and the head of its Educational Statistics and Analysis Division says that from what he has seen, British students are still more likely to graduate than those in most other countries. Even so, HESA's figures were greeted with dismay.

Dropout rates certainly can be kept down: Cambridge graduates nearly 98% of all the students it admits, the highest proportion in the country. This is largely a result of rigorous selection: more than 14,000 applicants chase 3,300 places each year, and almost every student accepted has top A-level grades. Universities that take students with lower grades and admit a larger share of those who apply are more likely to lose some of them along the way.

Traditionally, British universities have taken care only to admit students who are very likely to graduate, and then marched them through their education in double-quick time. The American way is different. In 2004 Thomas Weko of the Higher Education Policy Unit, a think tank, compared dropout rates on both sides of the Atlantic. He describes the American system as one that allows flexible attendance and has low barriers to entry for students who are at highest risk of dropping out, such as those who are working, disabled or caring for dependents. As a consequence, only about two-thirds of American students who set out to study for a bachelor's degree end up graduating.

But the dropouts haven't wasted their time, because even part of a degree confers an advantage in the American job market—as Dr Weko says, “completing a degree is better than not, but something is better than nothing”. In contrast, a report by researchers at London's Institute of

Education suggests that British men who start a university course but don't finish it are worse off than those who never begin one in the first place.

Probably the only sure way to bring British dropout rates down would be to return to the days of restricted access to higher education. Instead, universities could make a virtue out of necessity, giving credit in stages and offering a variety of stepping off points. Otherwise, British students may conclude that nothing is better than something.

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High-rise flats

Slums in the sky

Sep 29th 2005 | SOUTHWARK
From The Economist print edition

Dealing with Britain's decaying tower blocks will be both tricky and expensive

AP

STANDING in a corridor on the fifth floor of a tower block on the Aylesbury estate in south London is a miserable experience. The wind whips along unending concrete walls that are uniformly grey and permanently damp (though the occasional vomit stain provides a splash of colour). The stairwells reek of urine and cheap disinfectant and the smell of decaying rubbish wafts from the disposal chutes. Cleaning up and repainting hardly seems likely to make a difference, except perhaps to provide a blank canvas for the next gang of graffiti artists. The estate is a grim monument to Britain's failed post-war experiment in social housing.

It is also, thankfully, not long for this world. On September 27th Southwark council decided to knock the estate down and replace it with new houses. Most of the estate's residents are happy at the prospect of being moved to better accommodation elsewhere.

But Aylesbury is only one part of a bigger problem. There are thousands of residential buildings of five floors or more in London, and thousands more dotted throughout Britain's other big towns. A combination of shoddy building standards and inadequate maintenance by impoverished local authorities means that many are now falling apart.

In the short term, the buildings can be improved by trying to make up for the years of neglect. Often this is done by privatising the maintenance work, with residents voting to transfer responsibility from councils to private companies. This leads to new paint jobs and cleaner hallways. But it is, literally, papering over the cracks and no solution to the long-term problem: ill-maintained and poorly built concrete towers have a short lifespan.

The complicated structural repairs needed to extend the towers' lives would be prohibitively expensive. Local authorities, which are perennially short of money, are unlikely to be able to

afford them. Employing private-sector firms to do the heavy work is a non-starter too, since the towers' residents are even less likely to be able to find the money to foot the bill. Some residents in Tower Hamlets, another of London's concrete jungles, have been charged up to £20,000 each for fixing their homes. As news of the potential cost spreads, people soon go off the idea. In 2001, 73% of Aylesbury's residents voted against a planned transfer to a private housing association.

Knockdown prices

Ultimately, the only option is to demolish the estates, yet that creates almost as many problems as it solves. Towers typically house an area's poorest inhabitants, often hundreds of them in a single high-rise. If councils choose to knock down entire blocks at once, finding somewhere else for them to live can strain the already-stretched supply of local public housing.

And while knocking down a tower block dislodges a lot of people, it frees up only a small plot of land on which to build new homes. Many of the towers were built in groups of three or more. That encourages councils to buy and demolish entire estates, since few people are likely to want to live in new houses built right next to decaying eyesores.

One alternative is for local authorities to consult with residents and take down the worst buildings one at a time. Often this involves allowing them to empty gradually, as flats are left vacant when families move out. That is cheaper than demolishing entire estates, and it has logistical advantages, too: a gradual trickle of émigrés is easier to manage than a sudden flood. But there is the risk that newly abandoned flats in half-full buildings could attract squatters, drug dealers or prostitutes, which would make life even more unpleasant than it already is for those residents who remain.

Ultimately, the only option is to demolish the estates, yet that creates almost as many problems as it solves

There are economic worries, too. During the 1980s and 1990s the Conservatives encouraged local authorities to sell council houses to tenants as a way of earning extra cash. Before councils can demolish the flats, they will first have to buy them back. After the boom in the property market over the past two decades that is an expensive proposition. A typical block of 80 flats in London could be worth £8m-10m, a big sum for cash-strapped councils—Southwark has an annual budget of only £436m, yet it is in charge of more than 600 blocks of flats.

One option is to wait for the market to decide when the buildings should come down. That's financially attractive for hard-up councils, but is sure to stir up political trouble. Council flats in tower blocks were typically sold on 125-year leases, despite the fact that the blocks themselves were designed to last for only 60 or 70. As the blocks approach the end of their lives, the value of the flats falls. The prospect of a private-sector buy-out at these reduced prices could lead to protests from residents who feel they have been short-changed by the government.

In the end, although housing is notionally a matter for local government, a combination of cost and political delicacy will probably force Whitehall to take the lead, just as it did in the 1950s and 1960s when most of these high-rises were built.

But there is still room for councils to do their own thing. In Hackney, another poor London borough, the local council discovered that, unlike the rest of the population, its elderly residents were quite fond of their tower blocks, since they felt more secure living high above street level. It granted a stay of execution to two of its high-rises, moved young families out, put a concierge on the door and filled the towers with retired people. Given the shortage of residential care homes for the elderly, it could be one way to solve a modern problem with an old one.

Bagehot

No place in the sun yet for Gordon

Sep 29th 2005
From The Economist print edition

Poor old Gordon Brown. Yet again Tony Blair has upstaged him

IN RECENT years, Labour Party conferences have developed a predictable pattern. In the absence of any great ideological struggles, save the occasional twitch of protest from unions with members in the public sector who get fed up with being constantly cajoled to change the way they work, the rivalry between Gordon Brown and Tony Blair dominates everything.

On Monday Mr Brown makes a speech that is invariably interpreted as a challenge to Mr Blair's authority. The following day Mr Blair makes a speech designed to show that his authority is still very much intact. At the end of the week, everybody goes home and life carries on much as before—Mr Blair serenely indifferent to Mr Brown's seething frustration.

This week it should have been different. It was, after all, the first conference since the prime minister's announcement in October last year that he would not fight a fourth election and the virtual anointing of Mr Brown as his successor during a difficult election campaign in which the chancellor conspicuously came to Mr Blair's aid. From the outset, the impression that Mr Brown sought to convey was that of power seeping inevitably from Mr Blair to himself. This time, rather than use his speech to exaggerate his differences with Mr Blair, he would reassure sceptical Blairites that as prime minister he would be no less resolutely New Labour than Mr Blair.

The intended effect, however, was the same: to speed up Mr Blair's departure. Mr Brown, along with everyone else in the government, wants an orderly transition. But he wants it sooner rather than later. By denying Mr Blair the excuse that he must cling to office to preserve New Labour's mission, he was hoping to heap pressure on the prime minister to announce a timetable for his eventual exit. Mr Blair might be allowed another year, perhaps even 18 months, but anything more, suggested Mr Brown's supporters, would be self-indulgent and jeopardise the party's chances of winning a fourth election victory.

Disappointingly for Mr Brown, by the end of the week he seemed further away from his ambition than at the start. Mr Brown's speech was not bad, but it was not good enough to secure what he sought. He duly re-established his New Labour credentials, though these should never have been in much doubt—the idea that Mr Brown has a left-wing agenda he wants Labour to revert to the moment he becomes leader is the stuff of Tory fantasies.

What he failed to do was convince Blairite ministers that he would be on their side in accelerating the involvement of the private sector in public-service delivery, particularly by increasing capacity and breaking down monolithic provision in health care and secondary education. Mr Brown insisted that the ethos of those employed by the state is uniquely virtuous, even though in many parts of the country their salary and benefits compare favourably with the private sector. He repeated a favourite phrase, “the public square is more than a market place”, ignoring the fact that it is invariably markets that bring vitality and usefulness to such spaces.

The chancellor also managed to sound slightly presumptuous when he revealed his plan to make a

near-regal progress through Britain over the next 12 months in preparation for power. Worse still, in his relentlessly pulpit-bashing style, Mr Brown seemed, as always, keener on flattering his party than challenging it. As leader, he might strike a very different note, but if his intention was to appear prime ministerial, he fell some way short.

The contrast with Mr Blair did further damage to the chancellor's cause. Mr Blair's speech was closely argued, rigorously constructed and almost devoid of rhetoric. He set out to show how a synthesis of Labour's values and his ideas could meet the threats and the opportunities of globalisation. He confessed that in almost every area of government, he now regretted he had not pushed reform further and faster—a subtle, unspoken rebuke to Mr Brown for too often opposing him. By expanding choice in public services, he was doing no more than trying to give to ordinary people what had always been available to the rich. He acknowledged that the downside of being in power for a long time was fatigue, but that the upside was experience.

A year ago, Mr Blair did indeed look tired, but now he seems almost dauntingly reinvigorated

A year ago, Mr Blair did indeed look tired, but now he seems almost dauntingly reinvigorated. Suddenly, Mr Blair's promise before the election that if returned he would serve a full term no longer seems quite so preposterous. If asked which of the two was fresher and more purposeful, on the basis of this week, the Martian would unhesitatingly plump for Mr Blair. Labour voters appear to agree. According to an ICM poll in the *Guardian* this week, a mere 13% of Labour supporters want to see the back of Mr Blair any time soon. What's more, there is relatively little Mr Brown can do to dislodge him. The chancellor knows well that any overt move against the prime minister would risk the kind of internal strife that still blights Tory prospects 15 years after the putsch against Margaret Thatcher.

We don't want to lose you, but we think you ought to go

And yet. Without any timetable for Mr Blair's exit, the party will remain in a state of suspended animation. Renewal in office—the theme of many of the conference fringe meetings—is almost impossible under a leader who is not going to fight the next election and who carries as much baggage as Mr Blair. A terrible result in next May's local elections will hollow out Labour's already thin activist base.

What is also painfully clear after this week is that until Mr Blair does go, it will be impossible for Mr Brown to emerge from his shadow. Paradoxically, it is Mr Blair's very dominance that makes it all the more essential for his party's electoral prospects that he does not stay to the bitter end.

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Economist.com BUSINESS

Russian oil

Oil's well that ends well

Sep 29th 2005 | MOSCOW
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Reuters

The logic behind a huge Russian oil deal

Get article background

IN ONE of the jokes Russians tell about Roman Abramovich, owner of Chelsea football club and until this week an oil tycoon, he complains that London is an expensive city. Punch-line: “He still can't buy it.” Mr Abramovich's adopted home city may be unaffordable. But he should now at least be able to splash out on a few more yachts and soccer players. On September 28th, he and his associates agreed to sell their 72.7% stake in Sibneft, Russia's fifth-biggest oil firm, to Gazprom, a state-controlled gas giant, for $13.1 billion.

The deal itself—Russia's biggest ever takeover—was hardly a surprise: half the lawyers in Moscow seem to have been working on it, and on the whopping loans from a consortium of western banks said to be financing it, for months. The process acquired an extra sense of inevitability when Vladimir Putin, Russia's president, said he was aware of it. Still, it raises two big questions—and one big mystery.

First, does the acquisition make sense for Gazprom? The company is already a monster, boasting 16% of global gas reserves and 20% of world output. Some, including some in Russia's government, which owns 51% of it, argue that it is already unwieldy enough.

Gazprom's answer is that it wants to become a world-class integrated energy company. As well as boosting its oil production, it is developing fresh gas-export routes to Asia and North America. And Sibneft's oil is cheap: at around $3 per barrel of reserves, $13 billion is moderately expensive by Russian standards, but still a give-away by international ones. Several foreign oil majors would

have gleefully snapped it up on the same terms.

But they were not allowed to do so. The role of foreign firms in the Russian energy sector is now strictly delineated: they can contribute expertise and capital to joint-ventures, but no longer secure the strategic foothold that BP managed when it, in effect, bought half of TNK in 2003. Gazprom is pursuing the Kremlin's ambitions as well as its own: to wrest back control of the energy assets flogged in the rigged privatisations of the 1990s.

So in reality, the only other possible buyer was Rosneft, a state-owned oil firm, with which Gazprom was supposed to merge earlier this year. That deal fell apart, after Rosneft acquired Yuganskneftegaz, a subsidiary of once-mighty Yukos that had been appropriated by the courts. The ostensible reason was Gazprom's aversion to the risk of litigation; unofficially, it was the struggle between different Kremlin factions over which of the two companies would be the vehicle for the energy take-back. By keeping Yugansk and its independence, the Rosneft clan won that one; this week, Gazprom levelled the score. Sibneft, however, comes with its own risk—an ongoing dispute with Sibir Energy, another firm, over the dilution of Sibir's stake in a lucrative Siberian oil field. “These people stole this asset from us,” says Sibir's chief executive.

The second question is: are the deal, and the trend it represents, good for the Russian oil industry, and Russia itself? After the Yugansk and Sibneft transactions, the share of Russia's oil production controlled by the Kremlin will approach one-third. The state also influences oil exports via its pipeline monopoly; Gazprom has monopolies both on gas pipelines and gas sales outside the former Soviet Union. True, the Russian government still has a weaker grip on the energy sector than the governments of many other petro-states. But as one Moscow-based tycoon puts it, the problem is not with state ownership per se, but with this state in particular. The growth of Russian oil-production has already drooped. More state oversight—meaning more graft and less efficiency—is unlikely to help.

The big mystery concerns Mr Abramovich, a man who is said to have got his start selling dolls in a Moscow market, and who with his associates controls Millhouse Capital, which formally held the Sibneft stock. Given the treatment recently meted out to some of his oligarchic peers—among whom, it is fair to say, he is not universally popular—it seems strange that Gazprom is paying the market price for Sibneft (and just after the company has approved a huge $2.3 billion dividend). It is obvious why Mr Abramovich should want to sell up before the election season in 2007 and 2008: as the jokes testify, he is less popular at home than in west London, and might be vulnerable to anti-oligarch populism. He has always had a special talent for Kremlin ingratiation: he looks set to stay on as governor of Chukotka, a grim Arctic region that he once seemed eager to quit. Still, why is Mr Putin, hammer of the oligarchs, letting him walk away with all this cash? With whom will he be sharing it? There are rumours.

Meanwhile, Mikhail Khodorkovsky, ex-boss of Yukos and a less lucky oligarch, last week saw his appeal against his imprisonment for various alleged offences predictably and speedily rejected. When he was arrested, Yukos was in the process of merging with Mr Abramovich's firm. Yukos still holds 20% of Sibneft, for which it paid $3 billion. If and when that stake is also seized by the courts, it may be sold to an Indian or Chinese company. Mr Abramovich and his friends kept the $3 billion. Another nice deal for the erstwhile boss of Sibneft.

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Sony

Stringing along

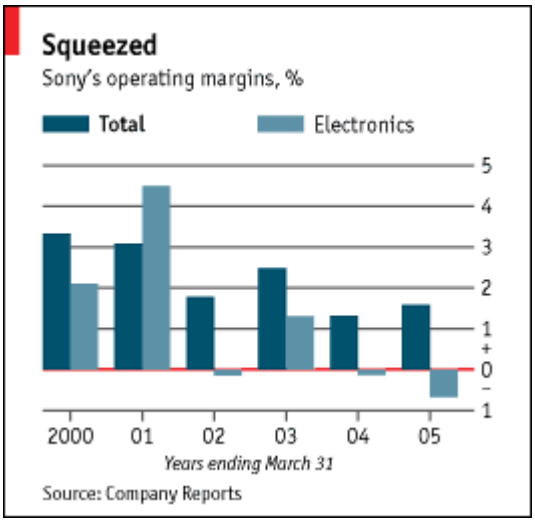
Sep 29th 2005 | TOKYO
From The Economist print edition

Timid reforms mean Sony's new boss is making two big gambles

Get article background

ONLY three months after taking over as the new boss of Sony, Sir Howard Stringer—the Welsh-American media executive who had previously run Sony's American unit—announced his new strategy. But analysts greeted the plan, unveiled on September 22nd, with disappointment. So Sir Howard was forced onto the defensive. American-style business rationalisation, he argued, was simply not possible in the more consensual and less brutal environment of Japan. Resistance from inside Sony had prevented him from doing anything too bold. Alas, the markets were unsympathetic: by early this week, Sony's shares had fallen by 6%.

Sony's problems are most obvious in its core electronics business, which accounts for two-thirds of its revenues. Consumer electronics devices such as televisions, DVD players and portable music-players have come under fierce price pressure, and the firm that once wowed the world with the Walkman and the Camcorder has failed to come up with any trend-setting new gadgets to boost profits (see chart).



Sir Howard has already ruled out one step that would reshape the company fundamentally: he insisted earlier this year that he will never break up Sony by dividing its media division (responsible for hits such as the "Spider-Man" films) from its electronics business. For now, therefore, he is pursuing the same vague, steady-as-she-goes strategy as his predecessor, Nobuyuki Idei, in which a phalanx of cost-cutting initiatives is flanked by some wishful thinking and a pair of bold gambles.

Sony will shut down 11 of its 65 plants around the world and shed 10,000 jobs, or about 7% of its workforce. It will also stop making a few unprofitable products, although it has yet to say which. Overall, the firm says, this will cut costs by ¥200 billion ($1.8 billion) by March 2008. That, says Sir Howard, will help to raise Sony's dismal operating-profit margins in electronics to 4%. Even this modest boost, however, depends on Sony meeting an ambitious target of increasing electronics revenues by 5% a year.

That is where the wishful thinking comes in. Sir Howard still says, as Mr Idei did, that Sony's position as a producer of entertainment content will somehow help it to sell gadgets more profitably. Sony has not only failed so far to demonstrate this, but its attempts have often involved proprietary standards that make its gadgets overly complicated and reduce their appeal to consumers.

Sir Howard will need that pair of gambles, therefore, to save the day. He is betting that two new products—video-disc players based on Sony's new “Blu-ray” high-definition standard, and the third generation of Sony's PlayStation gaming console—will become big hits with consumers. The Blu-ray standard, which had already been backed by big PC-makers like Dell and Hewlett-Packard, gained more adherents this year. But Toshiba's rival HD-DVD format, which is also in the running to succeed DVD as the dominant video-disc standard, is cheaper, and received fresh backing this week from Microsoft and Intel. Attempts to unify the two standards earlier this year came to nothing, so a bitter standards war, akin to the battle 30 years ago between the VHS and Betamax video-cassette standards, now seems inevitable. Sony lost the Betamax battle.

The PlayStation 3 also faces stiff competition. It will be the most powerful games console on the market when it launches next spring. But Sony's reliance on raw power to attract buyers looks less sophisticated than the approaches being taken by its rivals. Microsoft is using several new ways to sell its rival Xbox 360 console, such as a co-marketing deal with Samsung; Nintendo, meanwhile, is using innovative controllers and simpler games to reach out to non-gamers, like elderly people who want to sharpen their mental faculties.

Sir Howard's timid reforms mean that he is, in effect, betting that either Blu-ray or the PlayStation 3 will ride to Sony's rescue next year. If these bets do not pay off, he will have to do something far bolder to address Sony's resistance to change.

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Economist.com BUSINESS

Philips

In a new light

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With a new image, Philips promises new products

MAKING light bulbs has been a good business for Philips. They were the first thing Gerard and Anton Philips produced when they set up shop in 1891 in Eindhoven in the Netherlands. Now Philips, Europe's biggest electronics company and the world leader in lighting, is developing a new type of light which could consign the traditional bulb to history.

Incandescent light bulbs have not changed much over the years and still go pop and need to be replaced regularly. Consumers have shown only limited interest in more costly longer-life bulbs or fluorescent tubes, which are mostly unloved outside offices. But the new lighting Philips unveiled in Paris last week, as part of its ambitious re-branding, is completely different and "will change the whole character of the industry," claims Gerard Kleisterlee, Philips's chief executive.

Like its rivals, Philips is finding that slower spending by consumers and plummeting prices are making the consumer electronics market tough going. Hence the firm is looking for growth from other divisions, such as lighting and medical equipment. In its second quarter to the end of June, lighting sales grew by 4% to €1.1 billion ($1.36 billion) compared with the same quarter last year, and sales of medical systems were up by 6% to €1.5 billion. Consumer electronics sales in the same period shrunk slightly to €2.3 billion.

The new lighting that the firm is developing uses light-emitting diodes (LEDs). These are found as coloured indicators on electronic products. But LEDs have been getting more powerful and recent developments have led to high-intensity white-light LEDs. The devices will be more expensive, but compared to an ordinary light bulb, an LED light is more robust, consumes only one-eighth of the power, is cool to the touch and may not need replacing for ten to 20 years.

LED lighting is also much more flexible than the traditional light bulb. Philips's LEDs include bulb-shaped devices that fit directly into conventional lighting sockets. Some can be twisted or even squeezed to change intensity and colour. One type, called Chameleon, can analyse the colour of any object placed in front of it and change the colour of its light to match. Philips reckons such features could make LEDS an essential part of interior design. The lighting can also be incorporated into structures, including fabrics. Long life and low running costs will also make LEDs attractive in commercial applications and for public lighting.

The market for high-brightness LEDs, which includes devices like torches, is in its early stages. But it has been expanding rapidly and was already worth $3.7 billion last year, reckons Strategies Unlimited, a Silicon Valley research company. Philips thinks the market could soon be growing by around 25% a year. To bolster its position, the firm paid around $950m in August to acquire control of Lumileds, a pioneer in LED-lighting based in California.

Philips is coy about when its new range of LED lighting will be available, although Mr Kleisterlee insists that all the prototype products it displayed in Paris are close to production. These are among the first to be designed around the company's ambitious re-branding on the theme of

“sense and simplicity”. Philips, which has suffered from a staid image, is hoping stylish easy-to-operate products will help it stand out from rivals such as Sony and Samsung. If things go well, re-inventing the light bulb could do a lot more for the firm than simply boosting its bottom line.

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Economist.com BUSINESS

France and gardening

Come into the jardin, Maude

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A new business sprouts up in France

ALONGSIDE the out-of-town hypermarkets that ring French towns, a new species is spreading like ivy across the landscape: the suburban garden-centre. Offering everything from sturdy perennials to hardwood gazebos and citronella flares, brands such as Truffaut, Jardiland and Gamm Vert have taken root. Jardiland now has 106 centres across France, an increase of 33% since 2000. Gamm Vert has expanded its retail space by 20% since 2001. The French have traditionally been more passionate about trimming meat than privet hedges. So what is going on?

Gardening certainly seems to be blooming. Between 1999 and 2004, France's garden-centre market grew by 17%, to nearly €6 billion ($7.4 billion), says Promojardin, which promotes the activity. And the French are not just buying fairy lights for the terrace: the biggest category sold is outdoor plants.

What could explain this new urge? Despite Voltaire's famous maxim that "*il faut cultiver notre jardin*," gardening has never been a national sport in France, as it is in England. Newspapers do not devote pages to compost advice; there are no prime-time television garden shows promising to change your life with some decking and a water feature. Gardening in France has traditionally been either practical—the cultivation of vegetables—or a matter for the elite, its taste guided by the 17th-century formalism of André le Nôtre, who laid out the gardens at Versailles.

One explanation is suburbanisation. Promojardin says the number of French households with a garden had reached 61% by last year. Many others have at least a balcony or window box. Another factor could be that gardening, like organic food, has belatedly arrived as part of a broader ecological movement. "The return to nature has become fashionable," says Bérangère Lamboley, marketing head at Gamm Vert. The new buzzword at garden centres is *ludique*, or playful: gardening is fun. Truffaut's marketing stresses that gardening is therapeutic. "When you look after your plants, your worries disappear."

But perhaps there is another explanation. The expansion of garden-centres, says one retail-property investor, dates from 2000, when the former Socialist government brought in the 35-hour working week. With fewer hours in the office, and less money in their pockets, the French have taken to gardening as they have to DIY: as an inexpensive way to fill all that extra free time.

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Economist.com BUSINESS

Volkswagen

Keeping it in the family

Sep 29th 2005 | FRANKFURT
From The Economist print edition

Why tiny Porsche is buying into a car giant

WHY should a small and highly-profitable maker of sports cars suddenly hitch its fortunes to a lumbering and struggling mass-producer? That was the question that some alarmed shareholders asked this week when Porsche, the world's most profitable carmaker, announced plans to buy a 20% stake in Volkswagen (VW), Europe's biggest carmaker.

To some critics of the deal, Porsche's move looked like a return to cosy, German corporatism at its worst. Since January 2002, when a change in the law encouraged German companies to sell their cross-shareholdings in each other, free of capital gains tax, new foreign shareholders have often shaken up fossilised German management. A deal with friendly compatriots from Porsche might rescue VW from this distasteful fate, particularly since foreign hedge funds and corporate raiders had been rumoured to be circling VW. And indeed Porsche sources argued this week that a large part of their motivation in spending €3.3 billion ($3.96 billion) on VW shares was to prevent the giant being raided by hedge funds and broken up.

The impression of a cosy deal is strengthened by the historical and family ties linking the two firms. Ferdinand Porsche, commissioned by Hitler, designed the first Volkswagen beetle in the mid-1930s. His grandson, Ferdinand Piëch, ran VW from 1993 until 2002 and now heads its supervisory board; he sits on Porsche's supervisory board too. Two families related by marriage, the Porsches and the Piëchs, own all the voting shares of Porsche. They also own Porsche Holding in Salzburg, Austria, which is an important distributor of cars produced by VW-owned companies (including VW, Audi and Skoda) as well as by Porsche.

But there may also be some real business logic to Porsche's decision. Porsche argues that stability of VW ownership is crucial to its own long-term future. Porsche has common projects with VW, including chassis and body production of the Cayenne and Touareg sports utility vehicles (SUVs), and the development of a hybrid electric and fossil-fuel car; moreover, VW is already the source of about 30% of the components used in Porsche cars. More important still, Porsche is developing a four-door luxury saloon, called the Panamera, to be launched in 2009, which will compete head-on with models produced by its bigger German rivals Mercedes and BMW. Suddenly it will be in the big league, where the competition is getting tougher: this week Mercedes announced that it would have to cut 8,500 German jobs and take a special charge of €950m. For Porsche securing long-term economies of scale for sustained production is therefore seen as vital. A stable VW, despite its own struggles to become a lower-cost producer, could provide that.

But if the hedge funds moved in on VW, such stability might well disappear. That is because analysts agree that VW's break-up value is far greater than its present market valuation of around €16.5 billion. Its Audi subsidiary alone is arguably worth €10 billion, while Europcar (car hire) and Gedas (information technology) would fetch another €1.5 billion. VW Financial Services is a cash cow that produces close to €1 billion pre-tax profits a year. So hedge funds, which have reportedly been active buyers of the company's stock recently, were perceived as a real threat, particularly since a law protecting VW from takeover may soon by over-turned by the European Court of

Justice.

And if Porsche finds that VW is a millstone around its neck? Well then, the break-up value of the company limits the downside risk. In other words, if the going gets tough, Porsche could ditch its professed long-term plans and cash in its chips like a hedge fund.

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Economist.com BUSINESS

Regulating the drugs industry

The merry go-round

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From The Economist print edition

Why drug regulation is in a spin

Get article background

THERE are few industries for which regulation matters more than pharmaceuticals. And in the global drug industry—with annual sales of around $550 billion—no regulator matters more than America's Food and Drug Administration (FDA). America, the world's biggest market for drugs, is where companies prefer to launch new drugs, for which they need FDA approval. So the latest crisis at the FDA is a nasty blow to an industry already in pain from political attacks over drug prices and safety.

On September 23rd, the FDA commissioner, Lester Crawford, quit suddenly, after only two months in the agency's top job amid mutterings about his financial affairs. Congress had confirmed his appointment on July 18th, after dithering for six months, and only after the Bush administration had made last minute promises to Senator Hillary Clinton and others. These included a pledge that the FDA would vote by September 1st on whether to approve the over-the-counter sale of Plan B, a “morning-after” contraceptive pill. Once the job was his, Mr Crawford promptly broke that promise, dismaying many FDA staff who felt that politics had trumped scientific evidence. Susan Wood, the FDA's director for women's health, resigned, saying she could no longer work at the FDA, “when scientific and clinical evidence...has been overruled.”

The belief that science is paramount at the FDA is the agency's main asset in retaining the public's support, as it tries to balance its twin goals of allowing drugs to be sold only if they are safe, and of getting drugs that can improve or save lives to market as fast as possible. Accusations that the FDA has been sacrificing safety by approving drugs too fast, under pressure from profit-hungry drug firms, increased sharply a year ago, after Merck withdrew its Vioxx pain killer from sale. The FDA had approved the drug in 1999—but further trials had found that the drug increased the risk of heart problems in some patients. Some $27 billion was wiped off Merck's market value after the drug's withdrawal, and legal action is likely to cost the firm billions in compensation to Vioxx users. Meanwhile, the FDA is considering whether, and under what conditions, Vioxx and other similar drugs might return to the market.

George Bush's immediate response to the latest crisis at the FDA was to appoint as acting commissioner Andrew von Eschenbach, the head of America's National Cancer Institute (NCI). This prompted some grumbles, for Dr von Eschenbach is a friend of the president from Houston days. But he is also widely regarded as more than qualified to run the FDA. A bigger worry than his links with the president is that he will try to do the job, while staying in charge of the NCI. There is a real risk that, with a part-time boss, the FDA's debilitating leadership drift—it has had an acting commissioner during two-thirds of the Bush presidency—will continue.

But not everyone is gloomy. Robert Goldberg of the Manhattan Institute's Centre for Medical Progress says that the FDA is in far better shape than the headlines suggest. This owes much to Mark McClellan, Mr Crawford's predecessor, who in his year or so at the FDA introduced important

reforms designed to increase both the speed and effectiveness of the drug-approval process. As a result, says Mr Goldberg, the FDA has started to lead the drug industry rather than react to it, pointing it away from the money-spinning blockbuster mass-market drugs on which it has so long relied, towards more targeted drugs, suitable for some groups of patients but not all. That is an approach that Dr von Eschenbach has championed at the National Cancer Institute, including in joint projects with the FDA. He seems likely, if he can find the time, to continue the thrust of Mr McClellan's work at the FDA.

Mr Goldberg argues that there are other positive developments under way. “Vioxx may have been a tipping point in the industry”, he says, prompting the biggest firms to reconsider their past obsession with big-selling blockbuster drugs. Targeted medicine, however, requires a different approach to drug trials, which will need to focus more on understanding which groups of patients a drug works for. It will also need the FDA to ensure that the public properly understands the risks and benefits of specific drugs, especially those not suitable for everyone. The FDA would be better equipped to meet this challenge if it had a boss who is not only well respected, but full-time and expected to stick around.

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Economist.com BUSINESS

Online advertising

Pay per sale

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From The Economist print edition

The holy grail of advertising is within reach

“HALF the money I spend on advertising is wasted,” John Wanamaker, the owner of America's first big department store, allegedly said in the 1870s. “The trouble is, I don't know which half.” It has been the advertising industry's favourite witticism ever since. But it may expire soon, at least in the online world.

This week, Microsoft unveiled a new system for placing advertising hyperlinks on its MSN internet search site that could help it to close the gap with Google and Yahoo!, the two most popular search engines and the leaders in so-called “paid-search” or “pay-per-click” advertising. (MSN currently uses Yahoo!'s advertising technology.) The basic idea behind pay-per-click is that advertisers bid in an online auction for the right to have their link displayed next to the results for specific search terms—“used cars”, for instance, or “digital cameras”—and then pay only when a web surfer actually clicks on that link (hence “pay-per-click”). Since the consumer has already expressed intent—first by typing in the search terms, then by choosing the advertiser's link—he is more likely to make a purchase. From the advertiser's point of view, this reduces some of the waste that bothered Mr Wanamaker.

Pay-per-click advertising is the fastest-growing part of the advertising industry. In the first half of this year, it rose by 27% to $2.3 billion in America, the Interactive Advertising Bureau, a trade group in New York, said this week. That is 40% of all online advertising (though only 3% of total advertising) in America. Piper Jaffray, an investment bank, thinks that the pay-per-click market will grow to almost $20 billion within five years.

But pay-per-click is far from perfect. There is “click fraud”—bogus clicks generated by software-powered websites set up just for this purpose. And even humans who search and click often stop short of buying. Hence the next step: pay-per-call advertising. Most people first heard the term last month, when eBay, the world's largest online auction site, bought Skype, which makes software that lets people make free computer-to-computer phone calls. Meg Whitman, eBay's boss, explained that one rationale for the deal was to “monetise” Skype's internet telephony by placing little Skype “buttons” on web pages instead of sponsored text links. A web surfer might click on such a button and talk live to the advertiser's salesperson, at which point eBay would charge the advertiser.

A San Francisco company called Ingenio pioneered this approach in 1999 and already makes a decent living by placing toll-free numbers for local businesses on the results pages of search engines. This April, AOL, one of the big four internet portals, signed up as Ingenio's largest partner. The other three—Google, Yahoo! and MSN—will also launch pay-per-call programmes sooner or later, says Greg Sterling at The Kelsey Group, a market research firm, because small businesses and service providers like lawyers or plumbers find it much easier to close deals on the phone (many do not even have their own web sites). And faking calls is harder than faking clicks. Mr Sterling reckons that pay-per-call will be worth between $1.4 billion and $4 billion by 2009, on

top of pay-per-click revenues.

But even the pay-per-call model may turn out to be only an intermediate step towards the ultimate in advertising efficiency, which would be a pay-per-sale approach. This is what Bill Gross has recently started offering at SNAP, a search engine that he founded. United Airlines, for instance, places text links on SNAP's search pages, but it pays (about $10) not when somebody clicks or calls, but only when somebody actually buys a ticket. Eventually, argues Mr Gross, 100% of advertising will follow such a pay-per-sale approach—although he won't guess how soon—because this is “the holy grail of advertising.”

A bold claim, but credible, since it was also Mr Gross who invented the pay-per-click model in 1997 by launching the company that would become Overture, now part of Yahoo!, and whose business model Google imitated with spectacular success. His first innovation, says Mr Gross, merely liberated advertisers from the old “cost-per-thousand” model, in which they targeted audiences and then blindly threw money in their general direction. In this round, he says, he will liberate advertisers from all wasted spending, by tying their costs directly to real sales. Mr Wanamaker would be amazed.

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Computing

Cheap tricks

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From The Economist print edition

A $100 laptop for the poor could affect the computer industry

THE idea is as audacious as it altruistic: provide a personal laptop computer to every schoolchild—particularly in the poorest parts of the world. The first step to making that happen is whittling the price down to $100. And that is the goal of a group of American techno-gurus led by Nicholas Negroponte, the founder of the fabled MIT Media Lab. When he unveiled the idea at the World Economic Forum in January it seemed wildly ambitious. But surprisingly, it is starting to become a reality. Mr Negroponte plans to display the first prototype in November at a UN summit. Five countries—China, Brazil, Egypt, Thailand and South Africa—have said they will buy over 1m units each. Production is due to start in late 2006.

How is the group, called One Laptop Per Child (OLPC), able to create a laptop so inexpensively? It is mainly a matter of cleverly combining existing technologies in new ways. The laptop will have a basic processor made by AMD, flash memory instead of a hard disk, will be powered by batteries or a hand-crank, and will run open-source software. The $100 laptop also puts all the components behind the screen, not under the keyboard, so there is no need for an expensive hinge. So far, OLPC has got the price down to around $130.

But good news for the world's poor, may not be such great news for the world's computer manufacturers. The new machine is not simply of interest in the developing world. On September 22nd, Mitt Romney, the governor of Massachusetts, said the state should purchase one for every secondary-school student, when they become available.

Sales to schools are just one way in which the $100 laptop could change the computer industry more broadly. By depressing prices and fuelling the trend for “good-enough computing”, where customers upgrade less often, it could eventually put pressure on the world's biggest PC-makers.

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Economist.com BUSINESS

Face Value

A new pilot for Airbus

Sep 29th 2005
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Landov

Gustav Humbert is the first non-Frenchman to take the controls

Get article background

SEEN from Brussels, Berlin or London, Airbus is a fine example of European co-operation at its best. It is a shiny, profitable symbol of high technology, and a rare example of the old continent leading the world in a key industry. But to the French, the Toulouse-based firm is a national champion. When Gustav Humbert, a German engineer who has worked for Airbus for 25 years, succeeded Noël Forgeard, a Frenchman, as chief executive of the aircraft firm in June, he was the first non-Frenchman to get the top job at Airbus. The news was greeted with dismay in some sections of the French press. “Toulouse falls to the Germans”, screamed one headline.

Mr Humbert appears entirely unruffled by all the fuss. He acknowledges that, in succeeding Mr Forgeard, he has a hard act to follow. “Noël brought Airbus to a level of success that was unprecedented,” he says, truthfully enough. Under Mr Forgeard, Airbus was transformed from a design and marketing consortium into a single company. It snatched market leadership from Boeing, winning more orders and delivering more planes than its rival in recent years, while breaking the American firm's monopoly at the top end of the aircraft market—launching the super-jumbo A380 to rival Boeing's venerable 747. In the process it achieved profit margins superior to those of its competitor; a feat that was quite independent of its controversial state aid.

Flushed with this success, Mr Forgeard did his best to keep a tight control on Airbus even as he was promoted to become chief executive of its parent company EADS. In part, Mr Forgeard's actions simply reflected the reluctance of a dynamic boss to let go of a company that he had done so much to build. But it also fitted into a pattern of domineering French behaviour in Franco-

German business ventures that had already caused controversy in the pharmaceutical and engineering sectors—and provoked Gerhard Schröder, the German chancellor, to complain of French economic nationalism. The clash over the control of Airbus led to a bad-tempered boardroom row, which leaked into the press earlier this year. In the end, Mr Forgeard kept oversight of Airbus at EADS, but had to accept a German co-chief at EADS and a German boss of Airbus—Mr Humbert.

The contrast between the two men could not be sharper. The Frenchman has an obvious, impish sense of humour, a stage-French accent and a tendency never to miss a chance to get a rise out of Boeing. Mr Humbert's style is “international executive understated”—his wit is sardonic rather than uproarious. Not for him the provocative outbursts over the famous Airbus lunch table, designed to cause uproar thousands of miles away in Seattle. In barely accented English (the company language at senior levels) Mr Humbert suavely downplays the bitterness of the row with the Americans over state aid to Airbus, which has led to proceedings at the World Trade Organisation that will get under way this month, and expresses a hope for a negotiated solution. Mr Forgeard's Gallic urge to tweak the tail of the Americans is noticeably absent.

But the transition from Mr Forgeard to Mr Humbert will be about substance, as well as style. Under the Frenchman, Airbus was essentially a European champion, designed to counter the might of America's Boeing. Mr Humbert seems to be thinking of turning it into a global company that can counter an increasingly global Boeing. If his strategy takes wing over the next decade, the world aircraft market could turn into a battle between a European-Chinese conglomerate led by Airbus, and an American-Japanese alliance dominated by Boeing.

Hello world

This strategy could be portrayed as a break with Airbus's Eurocentric past. But it could equally be seen as part of the company's natural evolution. Airbus has already grown from a Franco-German joint-venture into a fully fledged European affair, with Britain and Spain as shareholders and Italy's aircraft industry a key supplier. Mr Humbert now sees his role as taking the company a stage further, and turning it into a truly global business. After taking over his first overseas visit was to China, where Airbus has a joint-venture—an engineering centre with a local aircraft manufacturer. The Chinese have been offered a 5% risk-bearing share of the new A350 mid-sized long-haul aircraft that the company will formally launch in the next two weeks. He envisages a similar arrangement to that which Boeing enjoys with the Japanese aircraft industry, which is due to build about a third of Boeing's new 787 aircraft in Japan.

Mr Humbert's vision of globalisation is based on pure pragmatism. “If we do not get China to contribute to our aircraft, then we are not going to get our aircraft into China,” he says. He sees more such collaboration with local partners in India and Russia, both of which are potentially huge markets for Airbus planes. In the short-term Airbus's new boss has been fortunate enough to take over at a time when demand is strong. Globally, aircraft orders look set to top the record 1,631 seen in 1989—with 375 deliveries for Airbus alone. The company is busily recruiting engineers in Europe to deal with expansion and new product launches. It needs 1,000 new people to deal with delays and cost over-runs on the A380.

But when he looks over the horizon, Mr Humbert sees much of the firm's future growth being absorbed by joint-venture partners and other suppliers outside Europe. Airbus even plans a factory in Louisiana to build air-refuelling tankers for the American air force. The sight of a “European” industrial champion manufacturing planes inside the United States for the American military might baffle nationalists in both France and the United States. But it would make sound business sense for Airbus. And, fortunately for the company, that is what seems to matter most to Gustav Humbert.

The travel industry

Flying from the computer

Sep 29th 2005
From The Economist print edition

The internet has pitted travel agents against travel providers in an intense battle to win customers

Get article background

THIS year's travel season, now drawing to a close, has been busier than ever, despite strikes and terrorist threats. The number of people flying within America is expected to return to the level that existed before September 2001: more than 680m people flew on domestic flights there last year and by 2015 it could top one billion. European travellers are also making more trips—for the first time there were more than 1m flights last year at London's airports. More and more of those trips are being booked over the internet.

Freed from having to ring busy call centres or queue at high-street travel agents, consumers have gone online in droves to find flights, hotels, car rentals and other travel services, making travel one of the most successful forms of e-commerce. The industry was ideally suited to be an internet business. Most booking information already existed in computer systems, but it was used by clerks and not directly available to consumers. By designing websites that ordinary people could use, online travel agents were able to put product availability and price transparency at their customers' fingertips. “That was a real revolution,” says Dara Khosrowshahi, chief executive of Expedia, an American company that has grown into the world's biggest online travel agent.

Even though the online travel business is at most only ten years old, its impact has been enormous. After the September 11th terrorist attacks on America, online agents helped airlines and hotels overcome a worldwide travel slump by making bargains more visible to a greater number of people. And because the internet is the cheapest way to take a booking, low-cost airlines in Europe and America also encouraged—and in some cases required—customers to buy their tickets online.

As consumers became more accustomed to buying travel over the internet, suppliers had to join in too. “The internet has been one of our biggest drivers of change,” says Simon Parks-Smith, the head of product management for British Airways (BA). By taking bookings directly, suppliers avoid paying fees to agents. This, in turn, is encouraging the online agents to broaden the range of services they offer.

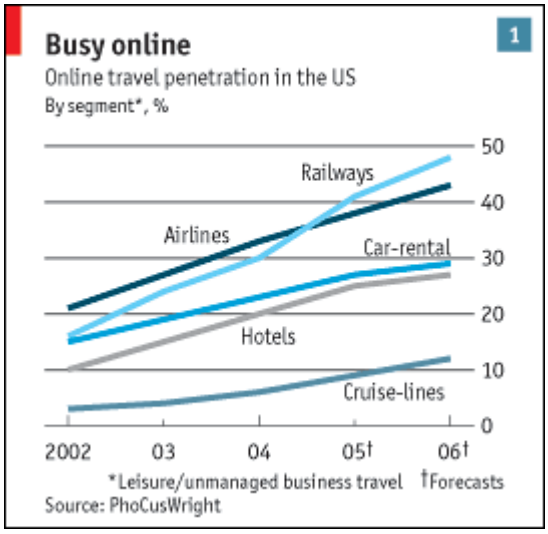
Such competition is good for consumers, provided it does not force the online travel industry to consolidate into too few hands. A wave of mergers and takeovers is indeed taking place as the internet's biggest travel agents expand into overseas markets, often by buying up smaller competitors. But ultimately the battle between travel suppliers and online agents will be decided by consumers, who will spend their money on the best prices and services that are available.

A lot is already known about how people like to shop online for travel. In America, 54% of consumers start with an online travel agent, such as Expedia.com, Travelocity.com or Orbitz.com, according to a study by Nielsen//NetRatings, which analyses internet use. The websites of travel suppliers, such as airlines and hotels, are visited first by 37% of shoppers. The other 9% start planning their trips using websites run by travel-search firms, such as Kayak.com and SideStep.com. These work like shopping comparison services: matching users' itineraries with offers and then directing bookings to the websites of agents and suppliers.

As with other forms of e-commerce, consumers tend to visit more than one website before they take out their credit cards. The typical American traveller looks at three websites before making a booking online, according to a study by PhoCusWright, a market-research company. Consumers surf around to check timetables, prices and frequent-flyer benefits and to read about resorts and hotels. In America, reckons PhoCusWright, suppliers and distributors currently each take about half of all online bookings.

That adds up to a sizeable chunk of the travel industry. Most analysts reckon about one-third of America's $200 billion travel market will be booked online this year. Some sectors, such as airlines, will see almost 40% of their bookings coming from the internet in 2005 (see chart 1)

To see more clearly what is happening, PhoCusWright breaks the travel market into two parts: leisure combined with “unmanaged” business travel (this is because individuals booking business trips can be indistinguishable from leisure travellers) and managed corporate travel (such as bookings made by specialist agencies working for a company). PhoCusWright predicts that the online part of the leisure/unmanaged business-travel market in America will be worth some $78 billion by 2006—having doubled in size since 2003. It expects the value of the managed-corporate market that goes online to be worth more than $36 billion by next year.



Many online agents are now expanding aggressively into the corporate market. With a series of bespoke services, they allow employees to make their own bookings online, but within the rules set by their employer. The services are proving popular. Expedia claims that as many as 85% of the corporate travellers offered a chance to book online through its site by their employers do so.

America's massive shift to online travel is being repeated in other parts of the world. Online services have yet to take off in the huge Asian market, which means that the potential there is

also huge. But in Europe they are growing rapidly. In the year to May, the number of visitors to travel websites in America grew by 12.7%, says comScore, a market-research company. This compares with an increase of almost 30% in the number of visitors to British travel websites. Whereas the percentage of Americans who look and then book has remained at a steady 3.7%, the booking ratio in Britain grew by 73% to 2.6%. Bob Ivins, comScore's European chief, says this shows that the American online travel business is maturing and turning into a battle for market share, whereas Europe's market is still blooming.

The wider availability of e-tickets should speed the development of online travel everywhere. It will spread even faster once paperless tickets become more widely accepted for so-called “interline agreements”, in which a ticket issued by one carrier is valid on another carrier for part of the journey. At present the members of the International Air Transport Association print 300m interline tickets a year. Giovanni Bisignani, the head of the organisation, hopes that all airlines will switch to e-ticketing by 2007, because it would save the industry a much-needed $3 billion a year.

Bigger and bigger

As online travel becomes more international, size begins to matter. Being big gives online agents advantages in cutting deals with suppliers and in spreading the costs of their operations over more customers. Smaller companies may not be able to afford the technical work needed to improve the functionality of their websites, whereas bigger sites that have the money can get a return on their investment much faster. This is also driving consolidation in the industry.

Expedia, which took $13.2 billion in gross bookings last year, was launched by Microsoft in 1996, but later sold to Barry Diller, a former Hollywood mogul, who has built a conglomerate of mainly internet companies. In early August, Expedia was spun out of Mr Diller's InterActiveCorp (IAC) as a separately traded public company. It contains other travel-related internet companies that IAC has bought, such as Hotels.com, Hotwire and TripAdvisor. Mr Diller believes that Expedia will operate more effectively and be valued more highly as a separate company. It already owns several websites in Europe and earlier this year bought a stake in eLong, a leading Chinese travel website.

Travelocity is owned by Texas-based Sabre Holdings, which also operates a global distribution and ticketing system used by airlines and hotels. On July 20th, Sabre bought Lastminute.com, Britain's best-known travel website, for £577m ($1.1 billion). Orbitz, the third giant, based in Chicago, was put together in early 2000 by a group of airlines as a way to sell directly to consumers. It was sold for $1.25 billion in 2004 to Cendant, a property and travel group based in New York. Cendant's other businesses include Galileo, a rival to Sabre's global distribution system; the Avis and Budget car-rental operations; and hotel chains such as Ramada and Days Inn. Earlier this year, Cendant also bought ebookers, a British online agent.

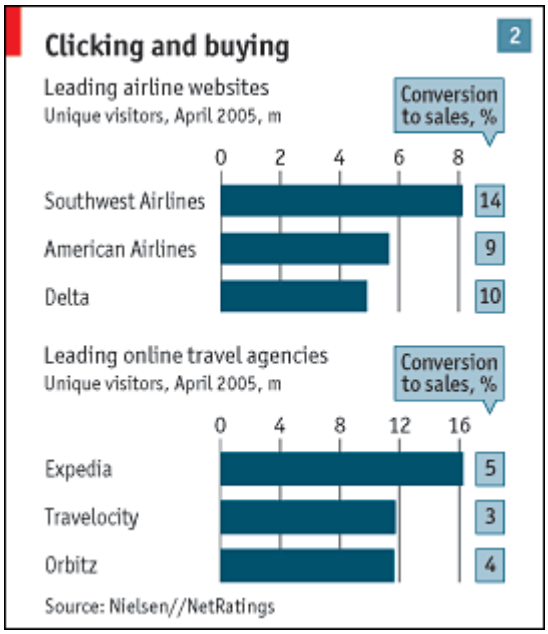
“The barriers to entry are a lot bigger than people thought in the beginning,” says Brent Hoberman, a co-founder of Lastminute and now chief executive of the combined European operations of Travelocity. Lastminute is a poster child of Britain's dotcom boom. Although it survived the 2001 bursting of the technology bubble, won millions of customers and ploughed some £25m a year into better technology and service improvements, it never made an annual net profit.

Mr Hoberman spoke to a number of potential suitors, but he says Travelocity impressed him because it is trying to get away from selling travel as a commodity. As well as travel, Lastminute provides restaurant bookings, gifts and tickets to events. Its website allows customers to do lots more than just arrange a trip.

That is a tactic others are trying. Creating a sense of community is an important way in which online travel agents will compete in the future, reckons Expedia's Mr Khosrowshahi. “So much of the travel experience depends on the hotel you stay in,” he adds. This is why his firm is providing a lot more information than just the ability to look at hotel amenities. Expedia allows users to rate hotels, write reviews and read the comments of other travellers.

Of course, the network effect also favours the big websites: the deeper the inventory and the greater the number of users, the more information a website will contain. Expedia is also trying to expand beyond the basics of travel and offer more destination services, such as a scuba-diving course or a sunset cruise.

As the online agents become travel cornucopias, more of those visiting their websites are planning and dreaming about trips and vacations, rather than dashing to buy a flight. A study by Nielsen//NetRatings of online-booking behaviour in America in April confirms this. Whereas the three biggest online travel agencies attracted up to twice as many website visitors as the three most popular airline websites, the airlines were able to convert a far higher proportion of visitors into sales (see chart 2). Many of the airlines' websites, of course, are visited by regular flyers who already know where they want to go and what flight they intend to catch.



Websites have already become the most important shop window for many airlines, hotels and car-rental companies. An example is ba.com. “It has transformed the way we sell our tickets and the way we stay in touch with our passengers,” says BA's Mr Parks-Smith. Because the internet has made it easier to compare deals, BA realised that users wanted to start by finding the lowest fare. “There was no point kidding ourselves about that,” adds Mr Parks-Smith. So people booking online are now presented with a range of fares to choose from, with the busiest flights commanding the highest premiums. Customers are shrewd enough to understand the laws of supply and demand, BA concluded.

Check out, check in

The airline is now making its website easier to use. The ability to check in and choose your own seat online has proved extremely popular, so a new facility to print your own boarding card at home is also likely to be a hit. Services such as booking rental cars, hotels and even guided tours at destinations will be added.

In this way, some travel suppliers' websites will come to resemble those of online travel agents. But how successful will airlines be at also taking hotel and car-rental bookings? Some airlines have long offered deals with so-called travel “partners”, so the idea is not completely new. However, in the past these deals have not always been the cheapest options.

If the prices of additional services offered by airlines are competitive, many travellers might prefer the convenience of a “one-stop” travel shop. But the choice of services offered by online agents may well be greater. And airlines and online agents will both be restricted in what they offer—they will not necessarily have distribution agreements with all the travel firms that operate in certain markets. This is particularly the case with some of the lowest-cost operators.

Ryanair, for instance, is Europe's biggest low-cost carrier. It no longer pays any commissions to travel agencies and now takes almost all its bookings directly, either via its own website or by telephone.

It is hard to imagine hotels and car-rental firms being successful at trying to sell flights, so their websites will probably remain specialised. But like airlines, these companies can also rely on various loyalty schemes to pull in online business. These schemes offer incentives to travellers to stay loyal to a particular brand, even if the price is a bit higher. When it comes to business travel, where the employer rather than the individual is paying, these incentives often succeed—making a booking via an online agent does not preclude a traveller from earning frequent-flyer points or other rewards, for example. However, the websites of airlines or hotels are likely to prove more popular with frequent travellers than those of online agents because the former can also be used to check up on rewards, cash them in and to find special offers, such as upgrades.

Another weapon many travel providers are likely to deploy are lowest-price guarantees. These are designed to persuade people that it is not worth looking any further for a better online deal. InterContinental, one of the world's biggest hotel chains and the owner of Crowne Plaza and Holiday Inn, claims to be the first hotel company to have introduced a price guarantee for every room booked through its own websites: if a lower rate can be found on the internet for the same accommodation on the same date, it will honour the lower rate and also give a 10% discount.

Big hotel groups are most able to flex their muscles this way, especially in America where the majority of hotel rooms are booked via chains. But in Europe smaller hotel groups and independent operators still dominate. These firms will be much more reliant on online agencies to bring them business.

The online agents also have an advantage with overseas visitors who may not know anything about the travel firms that operate in a country they intend to visit. The consumer reviews offered by online agents could become trusted guides. After all, you are unlikely to find anything damning written about the standard of service on the websites of travel providers.

In the middle are the specialist search websites that do not sell anything directly, but put consumers in touch with both online agents and travel firms. Cheapflights.com, for instance, asks travel firms to pay whenever a potential customer clicks through to an advertiser's website or clicks to obtain their telephone number. “There is still an awful lot of travel that can only be sold on the telephone,” says David Soskin, Cheapflights's chief executive. This could be because it involves complicated or special arrangements. Whereas Mr Soskin is convinced that the internet has persuaded people to travel more often, he also thinks the death of the traditional high-street travel agent has been greatly overstated.

Indeed, the more costly the trip, the more likely a traveller is to use a traditional travel agent. In America, according to Forrester, a research company, long-haul travellers spend 58% more than domestic leisure travellers, but are more than twice as likely to use an offline agent to book their trip. Henry Harteveldt, Forrester's online travel analyst, points out that even wealthy long-haul travellers are just as tantalised by low prices and many use the internet to research and plan their journeys, even though they may end up booking offline.

Will the contest between online agents and the websites of travel providers remain a draw, as it is now in America? There has always been commercial rivalry between travel agents and travel providers. But whereas it was initially the agents who developed the online market, the travel providers have caught up fast and are still beefing up their sites. With the ability to offer lowest-price guarantees and exclusive online services, such as picking your own seat in an aircraft, the travel providers may well move into the lead. And that could fuel yet more consolidation among online travel agents.

Nevertheless, the gap may not widen greatly. Both sides will still need each other, especially if the industry hits trouble in future as a result of economic slowdown or further terrorism. The online agents may then find their services are desperately required by travel firms scrambling to fill aircraft seats, hotels and unused rental cars. There is no doubt that the internet will become the standard way most people plan and book travel. But when it comes to making reservations, there is still plenty to play for. The ensuing competition will be great for consumers who want to hunt down travel bargains.

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Manufacturing employment

Industrial metamorphosis

Sep 29th 2005
From The Economist print edition

Factory jobs are becoming scarce. It's nothing to worry about

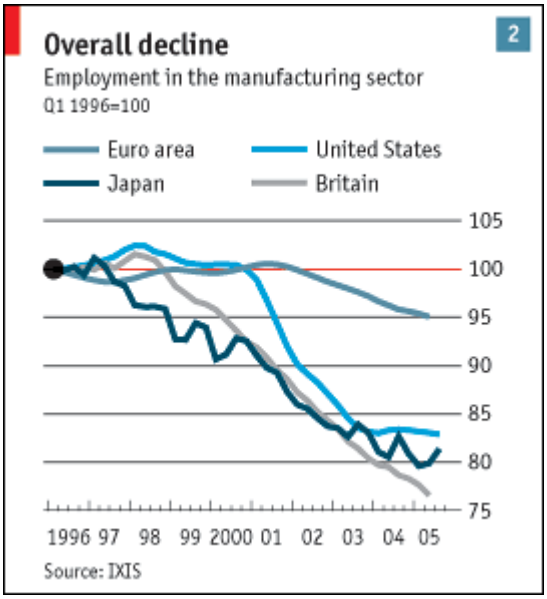
FOR the first time since the industrial revolution, fewer than 10% of American workers are now employed in manufacturing. And since perhaps half of the workers in a typical manufacturing firm are involved in service-type jobs, such as design, distribution and financial planning, the true share of workers making things you can drop on your toe may be only 5%. Is this cause for concern?

Our figure of 10% comes from dividing the number of manufacturing jobs—just over 14m, say the latest figures—by an estimated total workforce (including the self-employed, part-timers and the armed forces) of 147m. In 1970, around 25% of American workers were in manufacturing.

The share of manufacturing has also been falling in all other developed economies since 1970. The sharpest decline has been in Britain, where such jobs have dropped from 35% to 14% of the workforce (see chart 1). Indeed, the actual number of manufacturing jobs has fallen by half since 1970. The smallest drop has been in Italy, where manufacturing still accounts for 22% of employment. Germany is the only other big economy where more than one-fifth of workers are still in the business of making things. In Japan, the share has dropped to 18%.

Most people today work in services: in America, as many as 80%. But this trend is hardly new. As early as 1900, America and Britain already had more jobs in services than in industry. Even at its peak, early in the 20th century, employment in manufacturing never exceeded one-third of America's workforce.

What is new is the recent absolute decline in factory employment. Although manufacturing has long been shrinking as a proportion of America's expanding workforce, the number of industrial jobs stayed more or less the same between 1970 and the late 1990s. Since then, however, manufacturing employment has fallen in every year. Chart 2 shows that since 1996 the number of manufacturing jobs has shrunk by close to one-fifth in America, Britain and Japan. In the euro zone, the average loss has been only 5%.



Similarly, manufacturing output has fallen as a proportion of GDP (measured in current prices), although in most countries manufacturing's share of total production is slightly higher than its share of jobs. For instance, it currently makes up 13% of America's GDP, down from 26% in 1970. However, a closer look at the figures shows that the slide in manufacturing's share of GDP largely reflects a fall in the prices of goods relative to services. Measured in constant prices, the share of manufacturing in GDP has been broadly unchanged in America, and in developed countries as a whole, since 1980.

For all the bellyaching about the “decline of American manufacturing” and the shifting of production *en masse* to China, real output has been growing at an annual pace of almost 4% since 1991, faster than overall GDP growth. And despite China being widely acclaimed as the new workshop of the world, America remains the world's biggest manufacturer. Japan is in second place, with China a distant third, producing $700 billion-worth of manufactured goods, a mere half of America's total.

China has around six times as many manufacturing workers as America, but they are much less productive. And even China has not escaped the worldwide decline in manufacturing employment. Between 1995 and 2002 (the latest figures available) the number of such jobs fell by 15m in China, mainly due to the restructuring of inefficient state-owned enterprises. Manufacturing's share of employment has also been falling in Singapore, South Korea and Taiwan since 1990.

Since, contrary to conventional wisdom, manufacturing output has been growing strongly not declining, the fall in employment in America and elsewhere should be seen as a good thing. It does not represent a wholesale shift of production from developed economies to China. Instead, it largely reflects rapid productivity growth. And because unemployment rates in most developed economies have not increased during the past decade, even though manufacturing jobs have been lost, it would appear that most laid-off factory workers have found new jobs.

Deindustrialisation—the shrinkage of industrial jobs—is popularly perceived as a symptom of economic decline. On the contrary, it is a natural stage of economic development. As a country gets richer, it is inevitable that a smaller proportion of workers will be needed in manufacturing. The first reason is that households need only so many cars, fridges or microwaves, so as they become richer they tend to spend a bigger chunk of their income on services, such as holidays, health and education, rather than on goods.

Second, it is much easier to automate manufacturing than services, replacing men by machines. Faster productivity growth than in services means that manufacturing needs fewer workers. In turn, as workers move into more productive areas, this gives a boost to overall productivity and hence living standards.

From this point of view, the fact that manufacturing is still such a high share of jobs and output in Germany and Italy could be a symptom of economic weakness. Not only have both countries tried to protect manufacturing jobs with employment-protection laws, but a tangle of red tape also discourages the creation of new jobs in services. These two countries will therefore be more challenged by growing competition from emerging economies in years to come.

Any analysis of labour-market trends soon gets bogged down in a statistical swamp. For instance, a small part of the fall in manufacturing jobs is a statistical illusion caused by manufacturers contracting out services. If a carmaker stops employing its own office cleaners and instead buys cleaning services from a specialist company, then output and employment in the service sector appear to grow overnight, and those in manufacturing to shrink, even though nothing has changed.

A redundant distinction

More generally, the line between manufacturing and services is blurred. McDonald's counts as a service company, but a visit to any of its restaurants puts one in mind of an industrial assembly line, turning out cooked meat products. Similarly, an increasing slice of value-added in manufacturing consists of service activities, such as design, marketing, finance and after-sales support. Last but not least, Britain's number-crunchers stick *The Economist*, along with the whole publishing and printing industry, in manufacturing, even though almost all our staff are engaged in service-like activities.

The division between manufacturing and services has become redundant. A more sensible split now is between low-skilled and high-skilled jobs. Neither manufacturing nor services is inherently better than the other; they are interdependent. Computers are worthless without software writers; a television has no value without programmes. The issue is not whether people work in factories or not, but whether they are creating wealth. Manufacturing once delivered the highest value-added; high-tech industries, such as drugs and aerospace, still do. But in developed economies today, telecoms, software, banking and so on can create more wealth than making jeans or trainers. Writing a computer program creates more value than producing a computer disc.

Before long no one will much care whether firms are classified under manufacturing or services. Future prosperity will depend not on how economic activity is labelled, but on economies' ability to

innovate and their capacity to adjust.

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Economist.com FINANCE & ECONOMICS

The IMF and World Bank meetings

Bad loans made good

Sep 29th 2005
From The Economist print edition

Donors not debtors will repay the World Bank's bad loans

ALL the routes to the headquarters of the World Bank and the International Monetary Fund in Washington, DC, were blocked on September 24th and 25th by dozens of identical dumper trucks, the kind normally used to spread salted gravel on unpassable winter roads. Inside this heavy security cordon, the ministers and officials gathered for the Bank's and the Fund's annual meetings were busy clearing a path of their own.

Agreement was needed on a proposal to cancel the debts owed by the world's poorest countries to the Bretton Woods twins and the African Development Bank (AfDB). The proposal already had the backing of the G8 group of rich nations. Last weekend, according to Trevor Manuel, South Africa's finance minister and chairman of one of the key committees at the meetings, the G8 agreement "emerged as the G184 agreement", supported by the entire membership of the Fund and the Bank.

There are now 38 countries that the twins deem poor and indebted enough to warrant forgiveness. Between them, these countries owe $42.5 billion to the World Bank's soft-loan arm, $10 billion to the AfDB and $5 billion to the IMF. Eighteen of these countries have already jumped through the hoops designed to test their commitment to sound policies. Their slates may be clean by the end of the year.

Their debts, said Gordon Brown, Britain's chancellor of the exchequer and chairman of the IMF's ministerial committee, are unpayable. In fact, these countries are servicing their obligations, but only because the multilaterals offer them new grants and loans to help them repay their old ones. This recycling of funds keeps up appearances on the balance sheets of the Bank and the Fund, making bad loans look better than they really are. But it is also complicated and inefficient, consuming the time and energy of creditors and debtors alike.

The G8 proposal will end this elaborate charade. The Bank, Fund and AfDB will stop collecting debts and cut the flow of new money to these countries by the same amount. This much is an exercise in bookkeeping, not altruism. As Adam Lerrick, an economist at Carnegie Mellon University wrote recently, "All that debt forgiveness really needs is an eraser."

But there is more. Backed by the British, the Dutch and the Nordic countries, the World Bank has successfully convinced its donors to compensate it for writing off loans it could not have collected in full. This compensation is supposed to come on top of the regular contributions donor countries make to the Bank, such as the $18 billion already pledged for the years 2006 to 2008. Beyond 2008, however, it is impossible to know how much donors would have coughed up in the absence of debt relief. Therefore it is hard to gauge whether the money they offer will be in addition to, or instead of, money they would otherwise have given. In effect, the Bank has swapped the risk that poor countries will not repay their loans for the risk that rich countries will not redeem their promises.

To allay these fears, the G8 finance ministers all signed a letter to Paul Wolfowitz, the World Bank's new president, promising to compensate the Bank “dollar for dollar”. A “baseline” will be agreed, which is meant to define the counterfactual, showing what donor countries would have given had debt relief never happened.

It is not yet clear how this line will be drawn. Nonetheless, Mr Wolfowitz was happy to declare that “the path to complete debt relief now has been cleared.” Almost ten years after the multilaterals first consented to the partial forgiveness of their loans, the snow has finally melted.

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Economist.com FINANCE & ECONOMICS

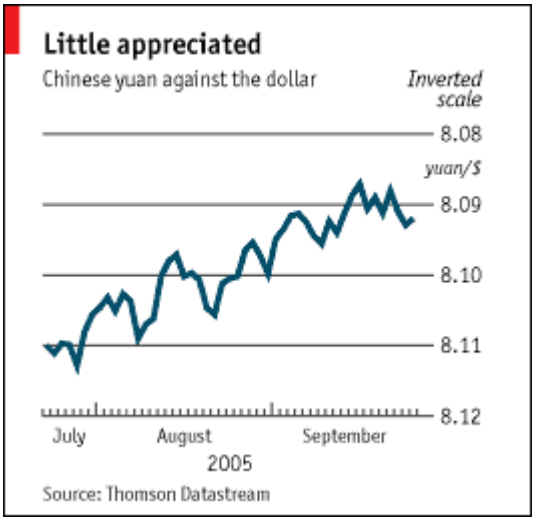
The yuan

Patching the basket

Sep 29th 2005 | HONG KONG
From The Economist print edition

China takes another tiny step towards a flexible currency

Get article background



SO NEW, and already there's a hole. Two months after abandoning the yuan's peg to the dollar for a link to a basket of several currencies, China has been forced to weave part of the basket again. On September 23rd, the People's Bank of China said that the yuan would be allowed to fluctuate by 3% a day against the euro, yen and other non-dollar currencies, compared with 1.5% previously. Daily movements against the dollar, meanwhile, remain limited to only 0.3%.

The reason for the change seems wholly practical. Under its old exchange-rate system, China controlled the yuan's value against the dollar, but allowed a fair bit of movement against other currencies. When it moved to a basket on July 21st—revaluing the yuan by 2.1% in the process—the corollary was tighter limits on daily fluctuations against currencies other than the dollar. But maintaining these has proved cumbersome.

Suppose that the euro jumps by 2% against the dollar in a day—a big move, but not unheard of. The European currency should then rise against the yuan as well. But it would not be possible to accommodate the full change within the 1.5% and 0.3% trading bands—unless the Chinese central bank could somehow nudge the dollar back up against the euro. Indeed, there have been rumours that over the past few weeks the monetary authorities have been using their copious foreign-exchange reserves to intervene in precisely this fashion.

Allowing non-dollar currencies to fluctuate by 3% gives the Chinese authorities a little more leeway, lessening the need for expensive intervention. It should also cut potential trading losses at designated foreign-exchange banks, because they can now hedge more effectively. It will also reduce currency speculation, if the wider bands are harder to put under pressure.

The timing of the change was also expeditious. Coming just before the meetings of the IMF, the World Bank and the G8 in Washington, DC, it allowed China to deflect charges that it is still frustrating a meaningful appreciation of the yuan. Since the peg was abandoned, the Chinese currency has risen by a mere 0.2% against the dollar (see chart).

True to form, the day the Washington meetings closed, on September 25th, the central bank made a further declaration: that it had no intention of changing the yuan's trading range against the dollar, in which 80% of China's foreign trade is settled. The tweaking of the currency basket so soon after its creation shows that market forces are having some impact on the yuan. Even so, it

will be a long time before China has a truly flexible currency.

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Economist.com FINANCE & ECONOMICS

Dubai's financial exchange

Do buy, do sell

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From The Economist print edition

A new stock exchange for the Middle East opens for business

WITH the world's tallest building, a man-made archipelago in the shape of the world and, coming soon, an indoor ski resort in the desert, Dubai is famous for its follies. On September 26th the Gulf emirate launched the Dubai International Financial Exchange (DIFX), which is meant to be a more serious venture.

The DIFX has started slowly. Its first securities are certificates linked to the world's main stockmarket indices and issued by Deutsche Bank, one of its founding members. In true Dubai fashion, though, it has grand aims: 15 initial public offerings, and as many secondary listings, in the next 18 months. There are plans to trade derivatives and Islamic bonds.

This is not the Gulf's first financial exchange. Indeed, Dubai itself already has one. Regional bourses have done well in recent years, fuelled by rising oil prices. Arab investors who once flocked to America have kept their money closer to home since September 11th 2001. But foreign investors find some of these exchanges hard to enter, owing to low liquidity and restrictions on ownership.

The DIFX aims to be different. It will trade in dollars, with no limits on foreign ownership and a low minimum listing requirement. It aims to allow companies to tap into deeper pools of capital than exist on the regional markets. Arab companies are its main target, but Indian and Chinese firms have also shown interest.

All this is part of a plan to make Dubai the financial capital of the Middle East. Three years ago the emirate began work on the Dubai International Financial Centre (DIFC), a 110-acre “state-within-a-state” with its own commercial laws based on international standards. More than 70 firms have permission to do business, in banking, trade finance, insurance, asset management and Islamic finance.

The success of the DIFC and its new exchange will depend in large part on how they are regulated. An independent regulator, the Dubai Financial Services Authority (DFSA), has been set up to draft and enforce regulations, with regulators from Britain and Australia. “We like to think we are user-friendly,” says one expatriate regulator. “The rule books are slimmer.”

But all has not run smoothly. Before the DIFC became operational last year, it sacked Ian Hay Davison and Phillip Thorpe, two experienced Britons, as chairman and chief executive of the DFSA. Mr Hay Davison claims that they were pushed out for objecting to interference from their bosses and to the same bosses' failure to disclose land deals at the centre. “Like so much in Dubai the appearance is often the point, and the appearance of having a regulatory environment exhibiting the highest international standards was seductive,” writes Mr Hay Davison in the current issue of *Euromoney*. “The reality behind creating such an environment was perhaps too much to absorb.”

The top people at the DIFC and the DFSA have since changed. Omar bin Sulaiman, current

director-general of the DIFC, says that there was a “misunderstanding”, adding: “It would have been disastrous if it happened during the operational phase.”

Alas, only last week new questions about corporate governance emerged. William Miller, the American ex-head of the exchange's audit committee, accused Lynton Jones, the chairman, and Steffen Schubert, the chief executive, of poor disclosure of a commercial conflict of interest. The management denies wrongdoing. But it is a spat Dubai could have done without.

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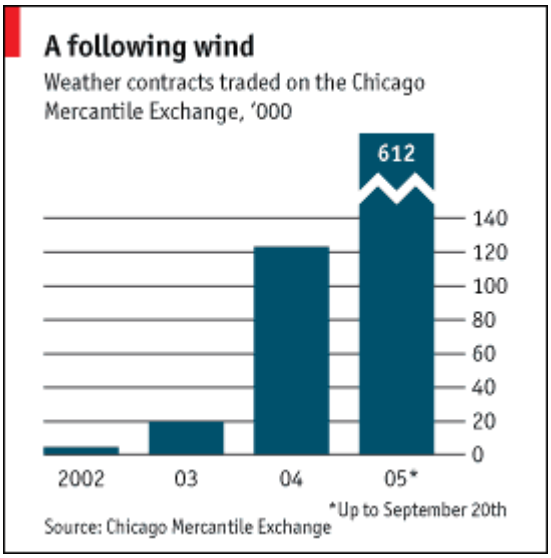
Economist.com FINANCE & ECONOMICS

Weather risk

Natural hedge

Sep 29th 2005
From The Economist print edition

Interest grows in financial instruments to offset swings in the weather



THE walloping dealt to America's Gulf coast by Hurricanes Katrina and Rita are but the most obvious reminders of the economic damage Mother Nature can inflict. Less spectacular weather often costs money too. This week, for instance, Britain's Meteorological Office gave warning that a harsh winter may be on the way—meaning higher fuel bills, disrupted journeys and lost days of work. Increasingly, however, companies are using clever financial instruments to shelter from the whims of the weather.

Weather-risk management contracts (or "weather derivatives") and natural-catastrophe bonds ("cat bonds") are two such devices. Firms use the former to offset the effects of variations in temperature, precipitation and wind speed on their businesses. Institutions from insurers to banks have been willing to supply cover. Cat bonds transfer some of the risk of unusual and devastating events from reinsurers to capital markets. Hedge funds have been keen investors in both these and weather derivatives.

The popularity of weather derivatives, which are traded both on exchanges and over the counter, has surged in recent years. Energy and agricultural firms are the biggest users, but even fizzy-drink makers have hedged against foul weather. Swiss Re, a big reinsurer, puts the value of weather derivatives at about $5 billion worldwide. At the Chicago Mercantile Exchange (CME), 612,000 weather contracts have been traded so far this year (to September 20th), up from 4,446 in all of 2002 (see chart). The CME's contracts cover 29 cities worldwide, focusing primarily on popular measures such as temperature.

There is also a widening array of customised weather-risk transactions. Stephen Doherty, of Speedwell Weather Derivatives in London, says that “exotic”, one-off contracts can be structured for, say, the number of days of frost at Amsterdam airport or the rainfall affecting a cherry crop. Having noted the effects of Katrina on some insurers, the CME is mulling over derivatives for big weather disasters as well.

For now, though, cat bonds are the instrument of choice for shelter from nature's full fury. These high-yield debt instruments work in tandem with insurance contracts. Investors buy the bonds; their money is put into a pot; specified levels of catastrophe trigger payments to bond issuers. The danger of losing all one's money means that most cat bonds are rated below investment grade and appeal only to those with an appetite for risk.

There are, however, plenty of investors eager for anything promising a decent yield. Judith Klugman of Swiss Re Capital Markets, a broker-dealer affiliated with the reinsurer, reckons the market for natural-catastrophe bonds has jumped from about $700m in 1997 to $5.3 billion today. The Gulf coast is not the only place where protection might be sought: companies have bought cover for Californian earthquakes and European windstorms.

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Economist.com FINANCE & ECONOMICS

Mobile phones and taxation

Making the connection

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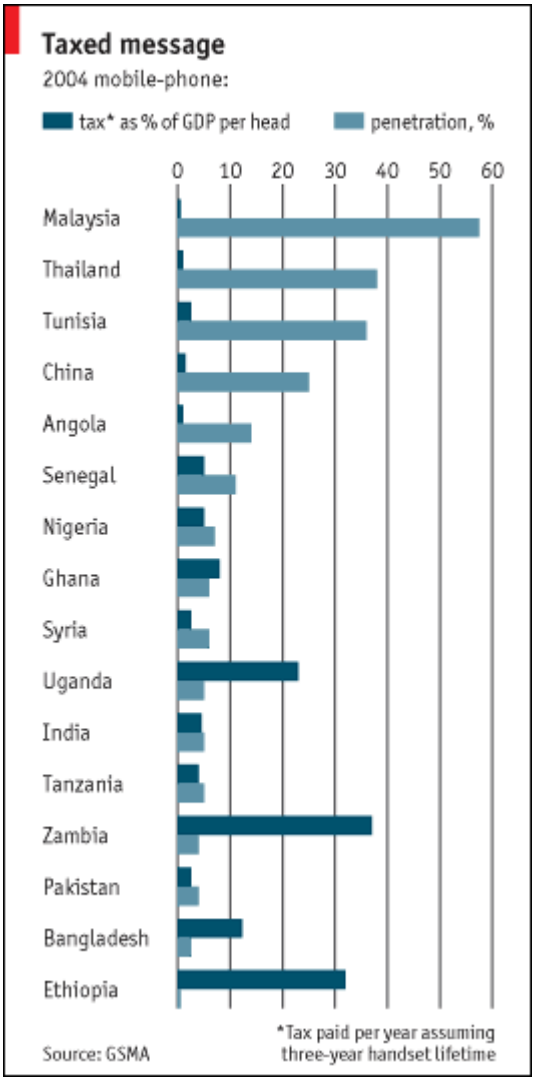
A new study examines the impact of taxation on mobile-phone adoption

THE global march of the mobile phone passed another milestone last month, when the number of devices in use worldwide went beyond 2 billion, according to Wireless Intelligence, an industry body. In a few rich countries, mobile devices now outnumber people. In the developing world, things are very different. Mobile phones are increasingly recognised as powerful tools in the fight against poverty, since they reduce transaction costs, facilitate entrepreneurship and substitute for slow, unreliable transport and postal systems. Annual subscription-growth rates of over 100% in many countries reflect the strength of demand. But the proportion of people with mobile phones is still very low—around 5% in India and sub-Saharan Africa—because phones are still beyond the means of the vast majority.

The mobile-telecoms industry, which is looking to developing countries for its next billion customers, is doing its best to cut prices. The price of a basic handset will have fallen from $50 at the start of 2004 to below $30 by next January, and below $20 by 2007.

But as prices fall, another barrier to adoption becomes more apparent: the taxes on mobile phones in many developing countries. A study released this week by the GSM Association, which promotes the use of the world's dominant mobile-phone standard, details the variation in tax policies and examines their effects. (The study was the work of four consultancies, Pyramid Research, Frontier Economics, Deloitte & Touche and Tarifica, and is endorsed by the International Telecommunication Union and the World Bank.)



Phones are taxed in many ways. Most countries charge value-added tax on handsets. Many also impose customs duties on imported phones (45.6% in Syria, for example, 33% in Ghana, 27% in Uganda, and $5 per handset in Bangladesh). Subscribers may face further taxes when they sign up ($14 in Bangladesh, $8 in Pakistan and Senegal, $24 in Turkey), as well as VAT on calls and, sometimes, additional telecoms-specific taxes too. All these taxes were added up, assuming average usage levels and a three-year life for each handset, to work out the tax paid each year by an average user in each of 50 developing countries. This figure, presented as a share of GDP per head, gives an indication of the burden of mobile-phone taxes.

Hardly surprisingly, developing countries with high mobile taxes generally have far fewer mobile phones per person than those with low taxes (see chart). Cutting taxes can boost adoption: India has reduced its handset import duties over the past three years, helping to boost penetration from less than 1% to more than 5%. Raising taxes can slow adoption: monthly subscriber growth in Bangladesh fell from 11% to 7% after the introduction of a $14 connection tax in June.

Of course, governments have to tax something, and mobile phones are convenient. The job of collecting taxes can be passed on to network operators, who already have to keep track of their customers' usage in order to charge them properly. In developing countries, mobile phones are often the top source of tax revenue, notes Ben Soppitt of the GSMA. But the cost of the taxes, in social, economic and developmental benefits forgone, is high. Most governments say they want to extend access to communications and close the “digital divide”. Special mobile-phone taxes have exactly the opposite effect.

So what is the best policy? The study makes no specific recommendations. But it does model the effects of various changes in tax policy. Scrapping all import duties and sales taxes on low-cost handsets (those costing below $30), for example, could prompt 930m additional sales by 2010. Although this would dent tax revenues in the short term, these new subscribers would pay an extra $25 billion to $45 billion in usage taxes over the same period. Less drastically, every reduction of one percentage point in sales taxes on mobile services would result in a 2% increase in mobile penetration between 2006 and 2010 in a typical developing country, the study predicts. Again, although tax revenue would be lost in the short term, it would rise eventually as more subscribers signed up. Cutting taxes and tariffs on handsets would also expand the tax base by increasing the proportion of legitimate handset sales; now, 40% are bought on the black market, according to Mark Williams of Frontier Economics.

But it is the special taxes on mobile phones, particularly on connections, that do most to deter adoption. Cutting these boosts subscriptions, broadening the tax base and offsetting the state's loss of revenue, Mr Williams remarks. It is “short-sighted” to single out such an important agent of development with punitive taxes, says Mr Soppitt. Taxes today or growth and perhaps even more taxes tomorrow? That is the choice—and the opportunity—that mobile phones offer.

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Auditors in Britain

Equitable outcome

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From The Economist print edition

At last, a happy day for accountants

CHEERFUL auditors have been hard to find recently, but there must have been a few sightings near London's High Court on September 22nd. Equitable Life, Britain's oldest mutual, dropped its negligence and breach-of-duty claim for £750m ($1.3 billion) against Ernst & Young, one of the world's "Big Four" accounting firms, and agreed to meet the defendant's pre-trial expenses.

The claim concerned the auditing of Equitable Life's guaranteed annuity policies between 1997 and 1999. Equitable Life, which had for many years made promises that it ended up being unable to keep, nearly collapsed five years ago. Defeat in court could have forced Ernst & Young out of business. Instead, after a three-year legal battle—not to mention the controversy that has dogged their profession since the demise of Enron in 2001—the auditors claimed victory.

Even so, other complaints against Big Four firms in Britain linger. Although these are before regulatory tribunals rather than courts, they remain important tests of public faith in auditors.

In September, the country's biggest accounting firm, PricewaterhouseCoopers (PwC), learnt that the new Accountancy Investigation & Discipline Board (AIDB), Britain's new overseer of auditors, had filed complaints against it to an independent tribunal. The complaints relate to PwC's 2002 audit of Mayflower, a busmaker that collapsed in 2004, and a subsidiary. Mayflower's shareholders received nothing when the company went under. If the tribunal finds an auditor at fault, it can impose sanctions from a simple reprimand to unlimited fines or loss of its auditing licence.

Deloitte & Touche may face a similar test. The AIDB is looking into its 2003 audit of MG Rover, a carmaker with a long history of financial problems, and its parent, Phoenix Venture Holdings. MG Rover went into administration in April this year and has since been sold to a Chinese carmaker, Nanjing Automotive.

Even Ernst & Young is not yet free of scrutiny. The Accountants' Joint Disciplinary Scheme, forerunner of the AIDB, filed complaints relating to its work for Equitable Life to a tribunal last year. The hearing was delayed until after the court case. "Clearly, we want to get on with it," says Christopher Dickson, executive counsel to the disciplinary scheme.

One reason why auditors are nervous about such complaints is that their liability is unlimited. Bodies such as the Institute of Chartered Accountants in England & Wales would like to see a cap on damages that can be sought from auditors. It is not, you understand, that the standard of British bean-counting is anything below the best: the institute points to a recent official report that found no "systemic weakness" in any firm.

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Economics focus

Currency competition

Sep 29th 2005
From The Economist print edition

How the dollar might lose its status as the world's main reserve currency

ONCE a decade or so, economists ask whether the dollar's reign as the world's number one reserve currency might be at the start of a slow decline. These musings usually coincide with a fall in the dollar's value. In the past 30 years, the dollar has had four bouts of marked depreciation. During the most recent, which began in 2002, it has fallen by 28% against the euro and by 14% against a broad basket of currencies. Even so, 66% of the world's official foreign-exchange holdings are still in dollars, compared with 25% in euros, 4% in yen and 3% in pounds, according to figures published last week by the IMF.

And yet dollar sceptics note that this time the dollar's crown is, if not wobbly, at least skewed. America's current-account deficit, at 6% of GDP, is its highest on record; its net foreign liabilities, at 22% of GDP, are also close to an all-time high. Foreign central banks seem to have reduced their purchases of American Treasuries: official holdings of these rose by only $2 billion in the first seven months of 2005, against $295 billion in (the whole of) 2004 and $175 billion in 2003. If this trend continues, other currencies could one day challenge the dollar's dominance.

History offers perhaps only one true example of a reserve-currency shift, from the British pound to the dollar. The pound was king during the era of the gold standard. But in the years after 1914, Britain switched from net creditor to net debtor, and by the 1920s the dollar was the only currency convertible to gold (although the pound returned to gold in 1925). Two costly wars and two episodes of currency devaluation in Britain later, the dollar was unchallenged as the world's chief reserve currency.

The likeliest pretender to the dollar's crown is the euro. Reserve currencies need to have a home economy with a large share of global output, trade and finance. America's economy still dominates, but the euro area is not much smaller. The euro area's total trade with the rest of the world is about as big as America's; about half of this trade is invoiced in euros. The financial market of the reserve currency country must also be deep, open and well developed. America leads the euro area by most measures, but the creation of the single currency has helped to integrate Europe's financial markets.

Confidence in the value of the currency is also an important requirement, and this is where critics of the dollar have mostly taken aim. Barry Eichengreen, of the University of California at Berkeley, argues in a recent paper* that whether the dollar retains its reserve-currency role depends mostly on America's own policies. If America allows its large current-account deficit to persist and its net foreign liabilities to rise, foreigners will become less willing to hold more dollars. The dollar would depreciate, creating inflationary pressure in America and making dollar reserves less attractive still—perhaps even if the Federal Reserve raised interest rates.

In another recent study†, Menzie Chinn, of the University of Wisconsin, and Jeffrey Frankel, of Harvard, estimate the importance of these factors in determining the shares of different currencies

in the world's total reserves. They also take “network externalities” into account: the tendency of each monetary authority to favour the dominant currency because all others do. They use these estimates to predict whether the euro could overtake the dollar as the world's main reserve currency.

It could, but not soon. Suppose, say the authors, that the dollar loses 3.6% a year against a basket of other currencies, while the euro gains 4.6% a year—the same rates as in 2001-04. Then, they reckon, the euro could become the top currency by 2024. If in addition Britain, Sweden, Denmark and all the central and eastern European countries that joined the European Union last year adopted the euro, it would supersede the dollar by 2019.

Of course, it is impossible to forecast such a change with any precision. The dollar, after all, took decades to displace the British pound. And the euro zone has obvious economic weaknesses. Moreover, with the stability and growth pact in a shambles and the EU constitution rejected by France and the Netherlands, some even wonder whether the single currency will be around in 20 years, let alone compete with the dollar.

Sharing the crown

Another view, offered by Mr Eichengreen, is that the world might eventually have more than one main reserve currency. The dollar could share its status if other currencies become more attractive. The preference to stick with the dominant currency might secure the greenback's position for a long time. However, as financial markets in other countries become more liquid, this effect is weakened and other currencies become more trusted as a store of value. Reserve-currency competition will then cease to be a game in which the winner takes all.

This process, thinks Mr Eichengreen, favours the euro. He is doubtful about other candidates, notably the yuan. He argues that both Europe and America “have strong institutions, respect for property rights, and sound macroeconomic policies relative to the rest of the world.” In China, by contrast, capital controls, financial markets that are neither very liquid nor transparent, and uncertainty about property rights make the yuan an unlikely contender for decades to come.

Whether the dollar ever loses or is forced to share its pre-eminence among reserve currencies depends mostly on whether America continues to run the economic policies that will eventually undermine its position. But even if America changes course, the crown may slip a bit.

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* “Sterling's Past, Dollar's Future: Historical Perspectives on Reserve Currency Competition”. NBER Working Paper No. 11336: www.nber.org/papers/w11336

† “Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency?” NBER Working Paper No. 11510: www.nber.org/papers/w11510

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Economist.com SCIENCE & TECHNOLOGY

Psychiatric disorders and immunity

Molecular self-loathing

Sep 29th 2005
From The Economist print edition

Anorexia and bulimia may be autoimmune diseases—and so may several other psychiatric illnesses

SOMETIMES, the immune system works in mysterious ways. During an infection one of its roles is to produce antibodies designed to attack and eliminate the invading bugs. However, in certain unlucky individuals the body also develops so-called autoantibodies which attack its own tissue, sometimes with devastating effects. The result is known as an autoimmune disease, two well-known examples of which are type-1 diabetes and multiple sclerosis. But there is a widespread suspicion among researchers in the field that a lot more diseases than these have an autoimmune component. In particular, they think, a number of illnesses usually labelled as “psychiatric” are actually, at bottom, the result of autoimmunity.

Until now, that suspicion has been based on correlations between certain sorts of infection and certain sets of psychiatric symptoms. But work just published in the *Proceedings of the National Academy of Sciences* by Serguei Fetissov of the Karolinska Institute in Stockholm and his colleagues has tied the connection more tightly for two psychiatric eating disorders—anorexia nervosa and bulimia nervosa.

Dr Fetissov's work suggests that abnormal levels of autoantibodies against hormones called melanocortins are a crucial part of the cause of these two diseases. Melanocortins are small protein molecules that carry messages between nerve cells in the brain. They are involved in regulating a variety of complex behaviours, including social interactions, stress responses and—most importantly in this context—food intake. So it is easy to see how interfering with them could cause anorexia and bulimia.

Shooting the messenger

To test this idea, Dr Fetissov and his colleagues analysed blood serum from three groups of women (both anorexia and bulimia are more common in women than in men). One of these groups consisted of people diagnosed as anorexic. The second was composed of individuals diagnosed as bulimic. The third contained people with no eating disorder.

The researchers looked to see whether there was any relationship between the levels of autoantibodies to melanocortins in these women and their expression of particular psychological traits—such as “Drive for thinness”, “Body dissatisfaction” and “Perfectionism”—which are associated with eating disorders and which can be measured using a specially designed scoring system.

What they found was intriguing. There was not one relationship, but two. The level of autoantibodies to melanocortins was positively correlated with anorexia, but it was inversely correlated with bulimia. These opposite correlations make sense. Although both disorders are associated with depression and self-doubt, anorexia involves a constant refusal to eat, whereas bulimia is a “diet-binge-purge disorder” that includes periods of excessive consumption. The molecular triggers of the two could thus easily be opposites.

The ultimate cause of the altered levels of autoantibody in anorexics and bulimics is unresolved as yet. However, according to the researchers, a clue may lie in the fact that micro-organisms, too, work in mysterious ways. In the world of bacteria and viruses, a strategy called molecular mimicry is common. In this, pathogens evolve to produce pieces of protein similar to those of their hosts, as a way of confusing that host's immune system. But the immune system is not always fooled, and in making antibodies to the “camouflage” proteins it sometimes turns out weapons that also attack the useful proteins that are being mimicked.

Two common gut bacteria, *Escherichia coli* and *Helicobacter pylori*, and also the influenza-A virus, are particularly adept at playing the evasive game of molecular mimicry, and the team is now looking at possible connections between different gut bacteria and autoantibodies against melanocortins to see if they can pin down which, if any, of these bugs might be responsible.

That is not to say, even if Dr Fetissov's idea is correct, that autoimmunity is the whole story. Both anorexia and bulimia are known to go hand in glove with particular personality characteristics which are not directly related to the disease. In anorexics, striving for perfection and conscientiousness are common non-pathological traits. In bulimics, such traits include risk-taking behaviour and problems with impulse control. So there appear to be predisposing factors at work, as well as the triggering effect of the autoantibodies.

Nevertheless, given the range of behaviours regulated by melanocortins and other, similar, messenger molecules, the suspicions that other psychiatric disorders—in particular, obsessive-compulsive disorder—are partly or wholly the product of a similar process seem entirely plausible. Dr Fetissov's work also adds weight to the idea that two other neurological diseases, schizophrenia and Tourette's syndrome, have an autoimmune component. In the case of these diseases, the damage seems to be caused irreversibly in the womb, suggesting that any autoantibodies involved are attacking structural molecules rather than messengers (attacks on structural molecules are the cause of multiple sclerosis, though they involve a different part of the immune system). That gives little hope for treatment. But in the case of anorexia, bulimia and, possibly, obsessive-compulsive disorder, Dr Fetissov's work opens a new line of thinking about how these diseases might be treated.

AIDS

A small hope

Sep 29th 2005
From The Economist print edition

In one part of Europe, HIV may be getting less virulent

Get article background

COULD HIV, the virus that causes AIDS, be weakening? The results of a study conducted in Belgium, at the Institute of Tropical Medicine in Antwerp, seem to suggest that in one corner of the world it might be. The report, published in the latest issue of *AIDS*, a specialist journal, concludes that HIV's ability to replicate (known technically as its virulence) may have decreased since the start of the pandemic. Kevin Ariën, the lead author of the paper, stresses that the study is based on a small set of samples and does not prove that HIV's virulence is attenuating around the world. However, it does offer new insights into the evolution of the disease.

Dr Ariën looked at 24 blood samples collected from untreated patients attending an HIV/AIDS clinic in Antwerp. A dozen of these samples were taken between 1986 and 1989; the other 12 were collected between 2002 and 2003. First, he analysed the samples to find their viral load (the number of virus particles per cubic centimetre) and the subtype of virus involved. In Europe and North America, the predominant subtype is B; in sub-Saharan Africa, where the epidemic is at its worst, the predominant subtype is C. Most of Dr Ariën's samples were of subtype B. Having done this analysis, he paired the samples off for a series of replicative “duels”. Each sample from the earlier series was matched with the most similar one from the later series, and they were placed in identical cell cultures to see which would multiply the most. The result was that 75% of the viruses from 2002-03 were less virulent than apparently similar counterparts from 1986-89—a statistically significant observation.

Dr Ariën's caution is sensible, at least until someone replicates the work elsewhere. But his conclusion is not necessarily surprising. Such viral attenuation, as it is known, is one way that vaccines are produced (viruses are passed from host to host in a laboratory, and the least virulent are selected for subsequent “passages” until what emerges is capable of stimulating the immune system without causing disease).

What causes attenuation in wild viruses, though, is a matter of speculation. Dr Ariën believes that in this case the attenuation could be the result of what he calls “serial genetic bottlenecks” during transmission from host to host. These act to reduce the genetic diversity (and thus the replicative fitness) of the virus. Genetic diversity is known to be an important component of HIV's virulence. But what might cause the bottlenecks is still unclear.

A second reason for caution besides the small size of the study is, as Geoffrey Garnett, a professor of microparasite epidemiology at Imperial College, London, points out, that the ability of a virus to infect cells in a test-tube is not the same as its ability to cause disease and death in a human host. Nevertheless, Dr Ariën's result is intriguing, and surely worth following up in a larger piece of research.

Economist.com SCIENCE & TECHNOLOGY

Alternative energy

The power of spin

Sep 29th 2005
From The Economist print edition

Harnessing artificial tornadoes as an energy source

WEATHER systems, as the world has recently been reminded, have awesome power. The energy released by a large hurricane can exceed the energy consumption of the human race for a whole year, and even an average tornado has a power similar to that of a large power station. If only mankind could harness that energy, rather than being at its mercy. Louis Michaud, a Canadian engineer who works at a large oil company, believes he has devised a way to do just that, by generating artificial whirlwinds that can be controlled and harnessed. He calls his invention the “atmospheric vortex engine”.

His idea works on a similar principle to a solar chimney, which consists of a tall, hollow cylinder surrounded by a large greenhouse. The sun heats the air in the greenhouse, and the hot air rises. But its only escape route is via the chimney. A turbine at the base of the chimney generates electricity as the air rushes by. A small solar chimney was operated successfully in Spain in the 1980s, and EnviroMission, an Australian firm, is planning to build a 1,000-metre-high example in New South Wales. But the efficiency of such a system is proportional to the height of the chimney, notes Mr Michaud, which is limited by practical considerations. His scheme replaces the chimney with a tornado-like vortex of spinning air, which could extend several kilometres into the atmosphere.

This vortex would be produced inside a large cylindrical wall, 200 metres in diameter and 100 metres tall. Warm air at ground level enters via tangential inlets around the base of the wall. Steam is also injected to get the vortex started. Once established, the heat content of the air at ground level is enough to keep the vortex going. As the air rises, it expands and cools, and water vapour condenses, releasing even more heat. This is, in fact, what powers a hurricane, which can be thought of as a heat engine that takes in warm, humid air at its base, releases cold, watery air at the top of the troposphere, about 12 kilometres up, and liberates a vast amount of energy in the process. (Just as water requires heat to make it boil, it releases heat as it condenses back into a liquid.)

Mr Michaud's vortex would reach a similar height to that of a hurricane, but its base would remain stationary. The intensity of the vortex would be controlled by closing the inlets around the base, or by opening another set of inlets to inject air in the opposite direction and so slow the vortex's rotation. And, of course, there would be a set of turbines at the base of the vortex that would allow its energy to be harnessed as air rushed through the inlets. Mr Michaud estimates that an atmospheric vortex engine with a diameter of 200 metres would produce around 200 megawatts of power.

Yes, but would it actually work? And if it did, could the resulting vortex really be controlled? Mr Michaud admits that the word “tornado” tends to worry people. This summer, 30 years after he had the original idea, and having failed to convince his employer or any other energy firm to take it on, he began tests at a site in Utah, with a cylindrical wall 10 metres in diameter. His initial aim is to demonstrate that artificial vortices can indeed be created and controlled. The next phase, he

says, would be to modify a cooling tower at an existing power station so that it uses a spinning vortex rather than the usual large fans to generate the necessary airflow within. The final step would be to add turbines to extract energy from the vortex.

Besides the engineering challenges involved, Mr Michaud must navigate the cultural divide between atmospheric scientists and the weather-modification community. The scientists regard the weather-modification crowd as cranks. They, in turn, cannot understand why the scientists are not taking a more hands-on, experimental approach to understanding the weather, rather than simply observing and modelling it. Mr Michaud has published nine papers in atmospheric-science and meteorology journals, and says his invention relies on principles that are consistent with scientists' current understanding of how natural weather systems work. So much for the theory. Now he must demonstrate that it works in practice.

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Economist.com SCIENCE & TECHNOLOGY

Mating behaviour

Swallows and amazons

Sep 30th 2005
From The Economist print edition

Male birds cannot afford to relax their standards

EVERYONE shows off when they are courting. But once you have paired up and settled down there is a tendency to let standards slip. That, however, may not be such a great idea—at least if you are a swallow. A study just published in *Science* by Rebecca Safran, of Princeton University in New Jersey, and her colleagues suggests that keeping up appearances after marriage is important.

Like many birds (though unlike most mammals) swallows form monogamous pairs to breed. Until genetic analysis became cheap enough for ornithologists to employ routinely, it was believed that this monogamy implied fidelity, and that the nestlings fed so assiduously by the male in such a partnership were, indeed, his. Alas, such tales are now known to be for the birds. Males are frequently cuckolded into bringing up the offspring of others. What is not known so clearly is what causes a female to cuckold her mate.

One possibility is the advantage of not, as it were, putting all her eggs in one basket. By getting her offspring fathered by more than one male she might spread her genetic risk. That, however, implies that she cannot assess this risk and plump for the best option. Another possibility, therefore, is that she can assess male quality very well, and will opt for a bit on the side if the bit in question is superior to the mate she has settled for. It was the second hypothesis that Dr Safran decided to test.

A bird's plumage is a good indicator of its condition. Growing brightly coloured feathers in the first place requires the right genes. Maintaining them requires health (ie, a good immune system) and grooming. In many bird species feather colour and position in the pecking order are closely correlated. Dr Safran therefore decided to manipulate her birds' feathers.

She observed a group of wild swallows, allowed them to pair up and lay eggs and then moved in. She took the eggs for analysis and took blood and feather samples from all of the adults. That enabled her to find out how many eggs in each clutch had been fathered by the male at the nest. She then divided the adult males into three groups. The first group had their plumage colour enhanced with a marker pen. The second group were “marked” with a pen that had no colour, to provide a control. The third group, which acted as a second type of control, were released without any marking. Pilot studies had shown that what might seem an obvious fourth procedure, to tone down, rather than enhance feather colour, was too damaging to work.

Swallows that lose their first clutch usually re-lay, and Dr Safran's birds duly did so. She allowed these eggs to hatch, then took samples from the nestlings to see who was the father.

The result was that the males who had had their plumage enhanced fathered a higher proportion of the clutches in their nests the second time round. In the case of the two control groups, the level of cuckoldry remained the same. The moral is clear. If you want to keep a demanding female faithful, dress and groom well.

California

America's dream, or nightmare

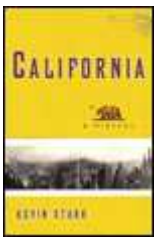
Sep 29th 2005
From The Economist print edition

Corbis

A classic history of the state that allows Americans to see their future

IF IT were a country, California would be one with more people than Canada and an economy the size of China's. Its scientists shoot, with their rockets, for the moon; its films spread Hollywood's culture around the globe; its athletes break world records; even its wines now rank with the best of France's. Somehow, it is always at the cutting edge, be it in the flower-power days of the 1960s or the dotcom boom of the 1990s. As Kevin Starr points out in his history of the state, California has long been "one of the prisms through which the American people, for better and for worse, could glimpse their future".

California: A History
By Kevin Starr



Modern Library; 400 pages; $24.95

Buy it at
Amazon.com

Mr Starr is too good a historian to offer any pat explanation; instead, he concentrates on the extraordinary array of people and events that have led from the mythical land of Queen Calafia, through the rule of Spain and Mexico, and on to the governorship of Arnold Schwarzenegger (what other state in America would have elected an iron-pumping film star with an Austrian accent?). Moreover, he does so with such elegance and humour that his book is a joy to read.

What emerges is not all Californian sunshine and light. Think back to the savage violence that accompanied the 1849 Gold Rush; or to the exclusion orders against the Chinese; or to the riots that regularly marked industrial and social relations in San Francisco (though dictionaries prefer Bavaria as the origin of "hoodlum", Mr Starr reckons it derives from young men invading Chinatown with the war cry "huddle them!"). California, it should be remembered, was very much the wild west, having to wait until 1850 before it could force its way to statehood.

So what tamed it? Mr Starr's answer is a combination of great men, great ideas and great projects. He emphasises the development of California's infrastructure: the extraordinary system of aqueducts and canals that transferred water from the north of the state to the arid south; the development of agriculture; the spread of the railroads and freeways; and, perhaps the most important factor for today's hi-tech California, the creation of a superb set of public universities.

All this, he writes, “began with water, the sine qua non of any civilisation.” He goes on cheerfully to note the “monumental damage to the environment” caused by irrigation projects that were “plagued by claims of deception, double-dealing and conflict of interest”: a state of affairs that was fodder for such Hollywood films as Roman Polanski's “Chinatown”.

One virtue of this book is its structure. Mr Starr is never trapped by his chronological framework. Instead, when the subject demands it, he manages deftly to flit back and forth among the decades (throughout the book, he is particularly good on the regular outbreaks of labour unrest, be it in the San Francisco dockyards or the fields of the Central Valley). Less satisfying is his account of California's cultural progress in the 19th and 20th centuries: does he really need to invoke so many long-forgotten writers to accompany such names as Jack London, Frank Norris, Mark Twain or Raymond Chandler?

But that is a minor criticism for a book that will become a California classic. The regret is that Mr Starr, doubtless pressed for space, leaves so little room—just a brief final chapter—for the implications of the past for California's future. He poses the question that most Americans prefer to gloss over: is California governable? “For all its impressive growth, there remains a volatility in the politics and governance of California, which became perfectly clear to the rest of the nation in the fall of 2003 when the voters of California recalled one governor and elected another.”

Tough for the Terminator

Indeed so, and Mr Starr wisely avoids making any premature judgment on their choice. Ills such as soaring house prices, gridlocked freeways and “embattled” public schools, combined with the budgetary problems that stem from the tax revolt of 1978 would test to the limit any governor, even the Terminator. As Mr Starr notes, no one should cite California as an unambiguous triumph: “There has always been something slightly bipolar about California. It was either utopia or dystopia, a dream or a nightmare, a hope or a broken promise—and too infrequently anything in between.”

California: A History.
By Kevin Starr.
Modern Library; 400 pages; $24.95

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America's armed forces

When the drums begin to roll

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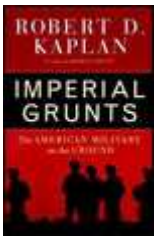
THE first problem with this book is its title. Noting that America's armed forces, the mightiest in history, divvy up the world between five regional commands (even before 2001, America had bases or basing rights in 59 countries), Robert Kaplan concludes that this amounts to a “global military empire”. He seeks to describe this empire through the experiences of the American servicemen defending it. It is a bold case, and he fails to make it.

Imperial Grunts: The American Military on the Ground
By Robert D. Kaplan



Random House; 448 pages; $27.95

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In most of these countries, the American military ventures that Mr Kaplan describes are too constrained by concern for national sovereignty to be truly imperial—a fact that is highlighted by his many specious comparisons between America's current military experience and Britain's 19th-century one. In the deployment of 175 Mongolian peacekeepers to Iraq, he finds proof that America “did, in fact, constitute a world empire.” Some empire, if so.

Mr Kaplan is most interested in the world as viewed by American foot soldiers—whom he calls “the cultural repositories of America's unique experience with freedom.” He provides fascinating detail on the composition and character of American forces—typically poor, patriotic and evangelical Christian. He writes fairly about their strengths: the controlled ferocity of marines; the more patient skills of Green Berets. And he is incisive in describing overall failings, including “Big Army” bureaucracy. At the same time he displays so much ignorance about the rest of the world, despite his extensive reading and travels, that it seems almost wilful.

Mr Kaplan's analysis is unsophisticated and unoriginal. Brave soldiers are often let down by malign politicians, diplomats and journalists. Soldiers, he suggests, may in their plain-speaking way understand the world better than those villains. He admires a bullish marine general who was “not interested in what was interesting, only in what mattered”.

In pursuit of “what matters”, Mr Kaplan never questions the official threats to American security: much of the Muslim world, he appears to assume, is heaving with international terrorists. He aggrandises things absurdly; for instance, he compares the mouldering remains of a bombed American barracks in the Philippines with the ruins of Angkor Wat. He divides the world into good and bad, and describes it accordingly.

Typical members of the poor world are “half-naked people with unreadable expressions”. An exception is Mongolia, America's grateful ally, where Mr Kaplan finds a shrine to Genghis Khan that has “a clean pagan simplicity”; the mosque-filled cityscape of Iraq's Fallujah he considers “truly ugly: the classic terrain of radicalism, occupied by the lumpen faithful.”

Interspersed with such nonsense, Mr Kaplan displays flashes of a better comprehension of

strategic issues: he is prepared to concede, for example, that blood-lusting American special-force fighters in Colombia were not best-placed to set national policy. Such moments of sense make the rest of the book even more unforgivable.

Imperial Grunts: The American Military on the Ground.
By Robert D. Kaplan.
Random House; 448 pages; $27.95

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Iraq's war

The step from hope to death

Sep 29th 2005
From The Economist print edition

FOREIGN correspondents, a breed not famous for modesty, seldom acknowledge how dependent they are on the translators and assistants who make their work possible. Michael Goldfarb, an American journalist with National Public Radio, has done more than acknowledge his debt to his Iraqi translator and friend, Ahmad Shawkat; he has written a vivid, poignant and sometimes angry book in his memory.

Mr Goldfarb uses Ahmad's life and death as a window through which to view Iraq's transition from tyranny to uncertain liberation. On the eve of the American invasion in 2003, he visits northern Iraq and meets Ahmad in a hotel lobby. The American and the Iraqi hit it off: both are secular liberals. Moreover Ahmad challenges the stereotypical view of three separate Iraqi communities: Sunni, Shia and Kurd. He is an assimilated, Arabic-speaking Kurd. As a young man he was drawn to Arab nationalism; then, when that light failed, to the ideal of a democratic Iraq where ethnic or confessional origin didn't matter.

Repeatedly imprisoned and tortured under Saddam Hussein, Ahmad dreamt of a free Iraq. He welcomed the American-led invasion and, with American help, set up in Mosul a newspaper and an institute to promote democracy. Then one day he was shot dead, whether by radical Islamists or ex-Baathists, or an unholy alliance of the two, is never determined. Mr Goldfarb, like his translator, had supported the war on the grounds that it was right to remove such an egregious dictator. But he is unsparing in his criticism of the botched peace and America's failure to prevent a slide into violence and sectarianism.

Ahmad's War, Ahmad's Peace: Surviving Under Saddam, Dying in the New Iraq.
By Michael Goldfarb.
Carroll & Graf; 349 pages; $25.95

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Economist.com BOOKS & ARTS

London

Rags and bones

Sep 29th 2005
From The Economist print edition

ONE of the oddest Victorian innovations was a top hat designed specially for theatregoers. This could be squashed flat during a performance, to avoid spoiling other people's view. But when the curtain fell, a quick bash against the seat in front released a spring mechanism, and the hat sprang into a more formal shape. It is a good illustration of the middle-class Victorian character—decorous, innovative, but also faintly ridiculous.

Liza Picard's fourth book on London is full of such innovations, as well as more useful ones, like sewers. A galloping run through the city takes in Highgate cemetery, gentleman's clubs, knackers' yards, conservatories, Mrs Beeton, beards and tuberculosis. Class distinctions are maintained as strictly as they were by the Victorians, with most chapters dealing first with the experiences of the poor, then the middle classes and finally the perfumed rich. A particularly good section on prostitution explains the differences between the brothel girls of the East End, the street walkers of the Strand and the *grandes horizontales* of the West End.

Victorian London: The Life of a City 1840-1870
By Liza Picard

Weidenfeld & Nicolson; 368 pages; £20

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The book, as its subtitle suggests, is not so much a history of London as a sketch—a “life” in the sense of a portrait. It does not strain, as most history books do, to see the past strictly through the eyes of those who lived through it. Modern judgments are cheerfully levelled against Victorian tastes in food, fashion and so on.

Another reason why the book is not a history is that it makes little attempt to explain how London evolved into its mid-19th-century form, or how the Victorian city influenced the modern version. On the rare occasions when a broader brush is used, the result can be messy. One of the author's wilder assertions is that before the advent of national railway timetables in the 1830s, every part of the country reckoned time in its own individual way. This is simply not true.

These are quibbles. Vividness is the book's aim, and this is achieved splendidly. We learn about the Victorians' sense of colour (they painted railings green, and thought orange and violet looked nice together) and the way they smelled, which was mostly offensive, in part thanks to their habit of washing silk in gin.

The overall impression is of a vibrant but tragic city. Victorian London was a place of extraordinary achievement. It produced the wondrous Great Exhibition, and advances in everything from mass catering to prison architecture. But, despite their cleverness and improving zeal, the inhabitants of that great metropolis were still ravaged by disease and by poverty so deep and wide that it would have shocked the Londoners of a century and a half earlier almost as much as it shocks us.

Victorian London: The Life of a City 1840-1870.
By Liza Picard.
Weidenfeld & Nicolson; 368 pages; £20

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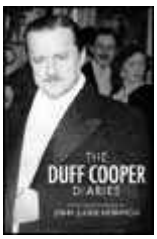
High society

Revelation without reflection

Sep 29th 2005
From The Economist print edition

ON FEBRUARY 2ND 1933 Duff Cooper writes: “I want to prevent this diary from becoming a mere record of luncheons and dinners—a fate which has overtaken all my diaries in the past.” He is unfair on himself, but only slightly.

The Duff Cooper Diaries
Edited by John Julius Norwich



Weidenfeld & Nicolson; 496 pages; £20

Buy it at
Amazon.co.uk

Cooper was a phenomenon. For nearly half a century after 1914, he was close to the centre of events in Britain, and since he was in turn a diplomat, soldier, backbench politician, cabinet minister, envoy to Charles de Gaulle's Free French and then Britain's post-war ambassador in Paris, he was often a participant in these events. He was clever and gifted, able to knock off a sonnet or a biography of Talleyrand without apparent difficulty. He was brave, showing considerable gallantry during his brief service in the first world war. And he could behave honourably, opposing the appeasement of Hitler and resigning as first lord of the admiralty over Munich. His aristocratic wife Diana was a celebrity, partly thanks to her great beauty, partly to her membership of a social set known as the “corrupt coterie”.

Whereas Diana was fond of morphia, the young Duff was prone to drink—and to gambling. More electrifying, though, even today, were his amorous activities. To the end of his life he was a compulsive philanderer. Strangely, this did not destroy his marriage, for he always loved Diana more than any other and she tolerated his affairs, sometimes with complicity.

Duff's attitude is well reflected by his entry for January 12th 1924, which describes how he spent much of the day reading Diana's old and new love letters to him (she is on the stage in New York at the time). He then adds, “I dined at the Embassy and brought Poppy [Baring] home with the inevitable result.” Diana, who periodically has her suspicions confirmed by reading his diary (sometimes he reads it to her), may complain or may actually encourage the affair. An awkward dinner in June 1945, at which Duff's evident interest in Daisy de Cabrol has fiercely wounded his current paramour, Loulou de Palffy, prompts a diary entry some days later that illustrates his wife's devoted complaisance. Loulou and Diana, it records, “spent this morning together and Diana told her she must go on loving me...She and I lunched together at the Méditerranée...”

With all these ingredients, the diaries should make a most delectable feast, every bit as good in fact as those that are described on almost every page. Yet they do not. The trouble is partly that discerned by Cooper himself: they are too much a record of meals eaten, people met (a name-dropper's delight) and places visited without much comment. More seriously, though, the comment, when it comes, is often not very interesting, even about Cooper himself; there is revelation, but not reflection. The middle part of the book takes a more serious turn and some events, such as King Edward VIII's abdication and the cabinet discussions of 1938, provide good passages, but the diary stops for most of 1926-36 and in 1939-44.

After 1944 the pattern of the diary reverts to meals, meetings and lechery, though there are interesting accounts of de Gaulle's prickliness and pettiness, and sometimes a piquant *bonne bouche*, such as this one, offered on March 20th 1944, about a former Vichy interior minister: “[Pierre] Pucheu was shot this morning. He met his death apparently with great courage, shaking hands with the firing squad and giving the order to fire himself.”

A further difficulty is that the diaries are intensely difficult to follow unless the reader has an intimate knowledge not just of British history but also of the politicians and pretty young things of the period. Most, though not all, people are given a bare-bones footnote on first mention, but you will have to carry in your head for many pages crucial details of the Alans and Patricks and Lionels and Eddies, never mind Daisy, Dollie, Poppy and the rest.

The book needs a pull-out list of the *dramatis personae* organised by Christian name. It also needs a much fuller (and corrected) index, to allow the dipper-in to make sense of it. Even more fundamental is the need for a guiding narrative to explain the context of the entries. The erudition of John Julius Norwich, Cooper's son, may have led him to assume that the only editing necessary was a winnowing of the entries. Not so. Too many events and places are unexplained and some references are misleading.

Would the work involved be worth the effort? Perhaps not. Prurient though it seems to say so, the book is chiefly notable for its catalogue of sexual conquests.

The Duff Cooper Diaries.
Edited by John Julius Norwich.
Weidenfeld & Nicolson; 496 pages; £20

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Economist.com BOOKS & ARTS

Contemporary dance

Those twisted, deconstructed bodies

Sep 29th 2005
From The Economist print edition

A revolutionary new ballet company from Frankfurt starts a world tour

ON THE stage at London's Sadler's Wells Theatre, four dancers are rehearsing. A palely muscled man with sad, noble features twists as if electrocuted, his body jolting into a lightning-fast sequence of dislocations. The same current races through the others, galvanising their bodies. Beyond the fierce gasps of their breathing, there is no soundtrack. Expended kinetic energy hangs in the air like gunsmoke. “Tighter!” comes a steady mid-Atlantic voice from the auditorium. “Condense it!” The sequence continues, then there is the sound of clapped hands, and the dancers come to a halt.

A trim figure in a grey sweater and corduroys appears on stage, the lights catching his rimless spectacles. “You guys,” he says, “you're doing it so fast it's illegible.” He turns to a woman in cherry-red shorts and pointe-shoes. “You need to stick your butt out more. Yup, like that.”

This is William Forsythe, an American choreographer and probably the most influential dance-maker working today. For two decades, until 2004, he was the director of Ballett Frankfurt, during which time he imprinted his dancers with a physical vocabulary more extreme than anything the dance world had seen before. In pieces such as “Steptext” (1984), “In the Middle, Somewhat Elevated” (1987) and “Herman Schmerman” (1992) he subjected classical ballet to a drastic process of deconstruction. Blasting away the conventional geometry, he introduced bizarre-seeming physical articulations, wrenching imbalances and vertiginous speed.

The results, especially when combined with the crashing electronic scores of Thom Willems, had a slick, dangerous sheen which was a world away from the “faux fantasy of decorum” into which, according to Mr Forsythe, conventional ballet had declined. And yet in essence his work never ceased to be balletic.

Born in 1949, he trained as a dancer in New York with Nolan Dingman, one of Balanchine's original dancers, and for many years immersed himself in the elaborately purist style that Balanchine acquired in the early years of the century at the Imperial Ballet school in Leningrad. The articulations that occur in his own choreography, Mr Forsythe explains in a borrowed Sadler's Wells dressing-room, are simply the logical extension of the Leningrad style. “This”, he says, standing to demonstrate the torsion of waist and shoulder-line that classical dancers call épaulement, “becomes this.” He increases the twisting until the position implodes, and a high-speed chain-reaction of adjustment and counter-adjustment is set in train. It is as if he were subjecting his classical dancer's body to chaos-theory.

In the 1980s and 1990s, Mr Forsythe and Ballett Frankfurt divided the dance world. Many were thrilled by the subversive power of works like “Artifact” (1984) in which, among other peculiarities, the front curtain repeatedly rose and crashed to the stage. They gleefully circulated the story of how, at the Paris Opéra première of “In the Middle, Somewhat Elevated”, Mr Forsythe had decided to “let the linear formations disintegrate” by informing the dancers just before curtain-up that he had reset the order of the sequences.

Other observers, however, were openly hostile to these cerebral adventures. One British critic, with a hyperbole that Mr Forsythe still relishes, described him as “the Antichrist of ballet”. Others, citing programme notes which referred to post-structuralist philosophy, algorithmic theory, and other arcana, declared the work chilly and obscurantist. In 1999 the New York critic Laura Jacobs described him in print as “pretentious as hell”, and suggested that he “get his nose out of Derrida and start tending to his *tendus*”.

Aficionados, however, insist that his work is passionately humane—you just need the key to understand it. Speaking of “Of Any if And” (1995) one of the pieces performed in London, Mr Forsythe describes how he created it shortly after the death from cancer of his wife, the dancer Tracy Kai-Maier. During the piece, a beautiful *pas de deux* to a suite by Mr Willems, in which the woman seems to be slipping away from the man, seemingly random words are raised and lowered on booms over the stage. There has been much discussion about their meaning. Mr Forsythe reveals that they are fragments taken from “De Rerum Natura” by the Roman author Lucretius, and concern the decomposition of the human body. On stage, the words are presented backwards, as if attempting by some alchemy to reverse the process, and it becomes clear that the piece is a lament; a cry of loss for Kai-Maier.

Not to be taken with dinner

Among those who failed to “get” Mr Forsythe's work were the councillors of Frankfurt. In 2002, they announced that the government-sponsored company was to be closed down in favour of a more conventional troupe. An instantaneous worldwide protest led them to reconsider this decision, but by then Mr Forsythe had decided to pack his bags. He no longer wanted to be answerable to patrons who, as he put it, “want ballet as part of the fine-dining experience”. In July 2004, after a long period of uncertainty, the curtain fell for the last time on Ballett Frankfurt.

In January 2005 the Forsythe Company was born. There are now 18 dancers instead of 36, their headquarters is no longer the Frankfurt Opera House but the city's smaller Bockenheimer Depot, and the company is financed by a private-public arrangement spread between the cities of Frankfurt and Dresden. The London season, which received whooping standing ovations every night, was the first overseas engagement of this phoenix-like entity, and the first engagement of a world tour that will take in Japan and Australia and terminate next May at the Brooklyn Academy of Music, New York.

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Economist.com PEOPLE

Obituary

Filiberto Ojeda Ríos

Sep 29th 2005
From The Economist print edition

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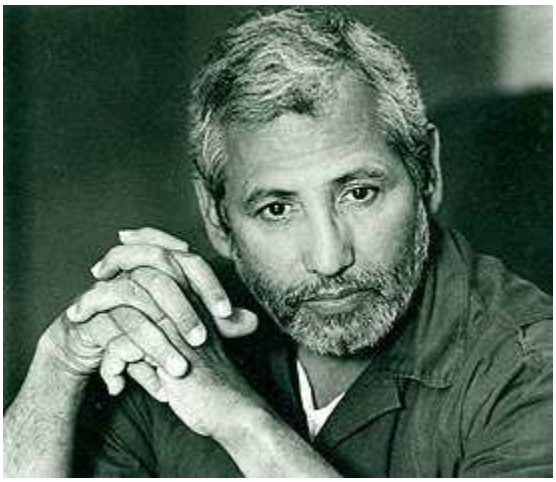

Filiberto Ojeda Ríos, Puerto Rican revolutionary, died on September 23rd, aged 72

PUERTO RICO is a not-quite-this, not-quite-that sort of place: a part of the United States but culturally and linguistically very Spanish, politically American but technically a “commonwealth”, not a state, whose people pay no federal taxes and have no vote in presidential elections. For some, this is a satisfactory equilibrium; for others, a half-way house on the way to statehood. For Filiberto Ojeda Ríos, it was a form of purgatory, an unwelcome condition between the hell of Spanish colonialism and the relatively celestial end-point of independence. But since independence was awkwardly neither desired by most Puerto Ricans nor offered by the other citizens of the United States, he would fight for it and, if need be, die for it. This he did, in a shoot-out with the FBI at a farmhouse in western Puerto Rico last Friday.

The incident made little impact in most of the country. Even in New York, which is home to over 1m people of Puerto Rican descent, it was reported only cursorily in the mainstream newspapers. The killing was noticed, though, in Hartford, Connecticut, and extensively covered by the *Hartford Courant*. No wonder: it was in West Hartford that Mr Ojeda Ríos had carried out his most notorious criminal act in the mainland United States, a raid upon a Wells Fargo depot in 1983 in which $7.2m was stolen. Only $80,000 was recovered. The rest was either spirited away to Mexico and thence Cuba to finance the struggle for Puerto Rican independence or, in a grand revolutionary gesture, scattered from the tops of tall buildings to protest against the “greed-infested men and mechanisms” exploiting ordinary Americans.

The raid was not all Mr Ojeda Ríos's work: he had acted with 18 members of the *Macheteros* (machete-wielders, or cane-cutters), an outfit he had formed in 1976. More formally known as the Boricua People's Army, they were an underground paramilitary group dedicated to freeing Puerto Rico from American “colonial” rule. Although they are said to have cells throughout the United States and even in other countries—the links with Cuba are supposedly strong—the *Macheteros*

have never been numerous. Their number these days is put at about 1,100.

Arrested in due course, Mr Ojeda Ríos was charged not just with involvement in the Hartford robbery but also with a rocket attack a few weeks later on a federal court in San Juan, Puerto Rico's capital. But strangely—for he had shot and wounded a policeman during his arrest, and was also implicated in the *Macheteros*' blowing-up of 11 aircraft at a National Guard base in Puerto Rico in 1981—he was constrained only by an electronic tag. This he cut off, and disappeared, becoming one of the FBI's "most wanted fugitives". Two years later, in 1992, he was sentenced *in absentia* to 55 years in prison.

Most Puerto Ricans had no liking for the methods employed by the *Macheteros*. Yet it was hard to dislike their leader. Unusually bright, Mr Ojeda Ríos had gone to university at the age of 15 and always showed an engaging intelligence. Former comrades who later gave up the struggle never lost their respect for him, and even FBI interrogators had a grudging admiration. Latterly he showed a single-minded dedication to his cause, yet he had other interests, notably music. His revolutionary career had been preceded by a stint in a well-known salsa band, for which he played both the guitar and the trumpet.

Perhaps all this helps to explain why the news of his death has been greeted more with sadness than anything else. There has certainly been no public rejoicing. Several hundred people gathered at a rally in Manhattan on September 26th, and a wake was planned in the *barrio* there later in the week. More significantly, in Puerto Rico itself questions have been asked about the circumstances of Mr Ojeda Ríos's death, and not just by his supporters. Governor Aníbal Acevedo Vilá, for instance, has described the FBI's actions as improper and highly irregular, asking why his government was not informed. Questions have also been asked by politicians across the spectrum about the time taken—the best part of a day—to fetch Mr Ojeda Ríos's body from the farmhouse after he had been shot. An autopsy has revealed that he did not die at once.

There is disquiet, too, about the timing of the shooting. It took place on the day of El Grito de Lares, the annual commemoration of the events of September 23rd 1868, when a group of Puerto Ricans rose up in protest against Spanish rule. It has become a date of great significance to the independence movement, and on it Mr Ojeda Ríos would sometimes, from a safe house, give interviews to Puerto Rican journalists.

In a second-class state

Yet if all this emotion owes something to the reluctant affection that some Puerto Ricans had for Mr Ojeda Ríos, it probably owes much more to the ambivalent sentiments widely held about his cause. Sympathy for violence there is not. But sympathy for a romantic who would fight for his little island and its 3.9m often-overlooked people, that is another matter. Like the Irish, an island nation of similar size, with a diaspora to match, Puerto Ricans often feel slighted by their big neighbour. Mr Ojeda Ríos drew on that sense of grievance, even though most of his countrymen were far too sensible to follow him.

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Overview

Sep 29th 2005
From The Economist print edition

Last year, American households borrowed almost $600 billion against the value of their homes to spend on other things, according to new research unveiled by **Alan Greenspan**, chairman of the Federal Reserve. Between a quarter and a third of this extra money is spent on consumption directly, Mr Greenspan said, and another quarter indirectly.

Mr Greenspan also said that the purchase of second homes, perhaps for speculative purposes, was playing an ever-bigger role in the **housing market**. Meanwhile, the median price of an existing home rose to $220,000 in August, up by 15.8% from a year before. This was the biggest annual price jump since 1979. Sales of new homes slowed, however. Units were sold at the rate of 1.24m a year in August, down by 9.9% on the previous month's pace.

America's Department of Energy reported that as much as 15% of the country's **oil-refining capacity** could be out of service for at least two weeks, thanks to Hurricane Rita and the lingering effects of Hurricane Katrina. **Consumer confidence** was also hit by the elements. The Conference Board's gauge dropped almost 19 points in September, hitting its lowest level since October 2003.

Revisions to **Britain's** GDP figures showed that the economy grew by 1.5% in the year to the second quarter, the slowest for 12 years.

In the **euro area**, M3, a broad measure of the money supply, rose by 8.1% in the year to August. The European Central Bank (ECB) believes annual growth of 4.5% is consistent with long-run price stability.

The ECB may be anxious, but the mood seems to be lifting in two of the euro area's biggest economies. In September, the Ifo index of **German** business sentiment was its highest since January, although the reading may not fully reflect this month's inconclusive election. Business confidence in **Italy** also rose unexpectedly, according to ISAE, a research institute. It posted its highest reading in September for ten months.

Japan's trade surplus, measured on a customs basis, shrank by 79.1% in the year to August, thanks to the higher cost of oil imports. Exports posted a healthy 9.1% gain over this period, but imports grew by 21.1%.

Consumer prices in **Canada** rose by 2.6% in the year to August, having increased by 2.0% in the year to July. Petrol prices soared by more than 20%.

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Output, demand and jobs

Sep 29th 2005
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q2	+ 5.2	+ 2.4	+ 3.2	+ 1.2	Q1	+ 1.6	Q2	5.0	Aug	5.7
Austria	+ 2.0	Q1	+ 0.8	+ 1.9	+ 2.0	+ 5.4	Jul	+ 1.7	Jun	5.2	Aug	4.9
Belgium	+ 1.5	Q2	+ 1.2	+ 1.2	+ 1.9	– 4.0	Jul	+ 5.9	Jun	13.5	Aug†	13.2
Britain	+ 1.5	Q2	+ 2.0	+ 2.0	+ 2.2	– 1.6	Jul	+ 0.8	Aug	4.7	Jul††	4.7
Canada	+ 2.7	Q2	+ 3.2	+ 2.8	+ 3.0	+ 0.4	Jun	+ 5.9	Jun	6.8	Aug	7.1
Denmark	+ 0.8	Q1	+ 0.6	+ 2.0	+ 2.2	– 1.6	Jul	+ 6.1	Jul	5.7	Aug	6.4
France	+ 1.3	Q2	+ 0.5	+ 1.4	+ 1.8	– 0.7	Jul	– 1.2	Jul	9.9	Jul	10.0
Germany	+ 0.6	Q2	nil	+ 0.9	+ 1.3	+ 3.0	Jul	– 3.0	Jul	11.7	Sep§	10.7
Italy	+ 0.1	Q2	+ 2.7	– 0.2	+ 1.0	– 0.9	Jul	– 1.5	Jun	7.8	Mar	8.2
Japan	+ 1.4	Q2	+ 3.3	+ 1.9	+ 1.9	– 2.3	Jul	+ 3.6	Jun	4.4	Jul	4.9
Netherlands	+ 1.3	Q2	+ 4.9	+ 0.5	+ 1.6	+ 0.1	Jul	+ 1.2	Jun	6.6	Aug**	6.2
Spain	+ 3.4	Q2	+ 3.6	+ 3.2	+ 2.8	– 3.5	Jul	+ 0.4	Jul	9.4	Jul	10.9
Sweden	+ 2.3	Q2	+ 2.6	+ 2.1	+ 2.7	+ 7.8	Jul	+ 6.2	Aug	6.5	Aug†	5.5
Switzerland	+ 1.0	Q2	+ 1.1	+ 0.8	+ 1.5	+ 3.9	Q2	+ 1.6	Jul	3.6	Aug†	3.7
United States	+ 3.6	Q2	+ 3.3	+ 3.7	+ 3.3	+ 3.1	Aug	+ 7.5	Jul	4.9	Aug	5.4
Euro area	+ 1.1	Q2	+ 1.2	+ 1.3	+ 1.7	+ 0.5	Jul	nil	Jul	8.6	Jul	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 0.2	Q2	– 6.3	na	na	+ 0.7	Jul	+ 5.4	Jul	7.2	Aug†	8.0
Greece	+ 3.7	Q2	na	na	na	– 4.5	Jul	+ 3.9	Jun	9.9	Mar	10.8
Iceland	+ 6.8	Q2	na	na	na	na		na		2.0	Jul†	3.0
Ireland	+ 2.4	Q1	+ 1.0	na	na	– 3.2	Jul	+ 4.9	Jul	4.3	Aug	4.4
Luxembourg	+ 3.1	Q1	na	na	na	– 1.5	Jun	– 1.4	Jul	4.4	Jul	4.0
New Zealand	+ 2.6	Q2	+ 4.5	na	na	+ 3.5	Q4	+ 5.9	Q2	3.7	Q2	4.0
Norway	+ 4.8	Q2	+ 5.2	na	na	– 1.3	Jul	+ 5.1	Aug	4.7	Jul‡	4.5
Portugal	+ 0.5	Q2	+ 4.1	na	na	– 0.8	Jul	– 1.9	Jul	7.2	Q2†	6.3

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††May-Jul; claimant count rate 2.8% in Aug.
§EU harmonised rate 9.0% in Jul. **Jun-Aug.

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Prices and wages

Sep 29th 2005
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2005	2006	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 2.5	Q2	+ 2.5	+ 2.7	+ 2.7	+ 6.9	Q2	+ 2.8	+ 5.8	Q2	+ 3.0
Austria	+ 2.0	Aug	+ 2.3	+ 2.1	+ 1.8	+ 0.9	Aug	+ 6.3	+ 2.3	Aug	+ 2.0
Belgium	+ 3.1	Aug	+ 2.3	+ 2.4	+ 2.0	+ 1.8	Jul	+ 5.5	+ 2.5	Jul	+ 2.2
Britain	+ 2.4	Aug*	+ 1.3	+ 2.0	+ 1.9	+ 3.0	Aug	+ 2.8	+ 4.2	Jul†	+ 3.8
Canada	+ 2.6	Aug	+ 1.9	+ 2.1	+ 2.2	– 0.3	Jul	+ 5.5	+ 1.4	Jul	+ 1.5
Denmark	+ 2.2	Aug	+ 1.2	+ 1.6	+ 1.8	+ 5.0	Aug	+ 3.1	+ 2.9	Q2	+ 3.1
France	+ 1.8	Aug	+ 2.4	+ 1.8	+ 1.6	+ 2.8	Aug	+ 2.8	+ 2.9	Q2	+ 2.8
Germany	+ 2.5	Sep	+ 1.8	+ 1.7	+ 1.6	+ 1.9	Aug	+ 4.2	+ 1.3	Jul	+ 0.4
Italy	+ 2.0	Aug	+ 2.3	+ 2.1	+ 1.9	+ 3.6	Jul	+ 3.3	+ 2.9	Aug	+ 2.6
Japan	– 0.3	Jul	– 0.1	– 0.1	+ 0.3	+ 1.7	Aug	+ 1.7	+ 3.7	Jul	+ 1.7
Netherlands	+ 1.8	Aug	+ 1.1	+ 1.4	na	+ 5.6	Jul	+ 5.2	+ 0.9	Aug	+ 1.0
Spain	+ 3.3	Aug	+ 3.3	+ 3.2	+ 2.9	+ 4.9	Aug	+ 4.4	+ 3.4	Q2	+ 3.1
Sweden	+ 0.6	Aug	+ 0.6	+ 0.5	+ 1.3	+ 4.2	Aug	+ 2.0	+ 2.6	Jun	+ 1.6
Switzerland	+ 1.0	Aug	+ 1.0	+ 1.1	+ 1.1	+ 1.0	Aug	+ 1.5	+ 0.9	2004	+ 1.4
United States	+ 3.6	Aug	+ 2.7	+ 3.0	+ 2.7	+ 5.1	Aug	+ 3.4	+ 2.7	Aug	+ 2.2
Euro area	+ 2.2	Aug	+ 2.3	+ 2.1	+ 1.8	+ 4.0	Jul	+ 2.9	+ 2.3	Q2	+ 2.1
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.9	Aug	+ 0.4	na	na	+ 3.8	Aug	+ 1.8	+ 4.0	Q2	+ 3.8
Greece	+ 3.7	Aug	+ 2.7	na	na	+ 5.1	Jul	+ 4.7	na		na
Iceland	+ 4.8	Sep	+ 3.4	na	na	+ 4.6	Sep	+ 5.2	+ 6.7	Aug	+ 5.2
Ireland	+ 2.3	Aug	+ 2.6	na	na	– 1.1	Aug	– 0.4	+ 6.4	Q1	+ 3.9
Luxembourg	+ 2.7	Aug	+ 2.3	na	na	+ 4.2	Jul	+ 9.8	+ 1.6	Jun	+ 2.8
New Zealand	+ 2.8	Q2	+ 2.4	na	na	+ 4.7	Q2	+ 1.5	+ 2.6	Q2	+ 2.3
Norway	+ 1.9	Aug	+ 1.0	na	na	+19.9	Aug	+16.4	+ 3.8	Q2	+ 4.1
Portugal	+ 2.6	Aug	+ 2.3	na	na	+ 4.4	Aug	+ 4.0	– 0.2	Jun	– 0.1

*RPI inflation rate 2.8% in Aug. †May-Jul.

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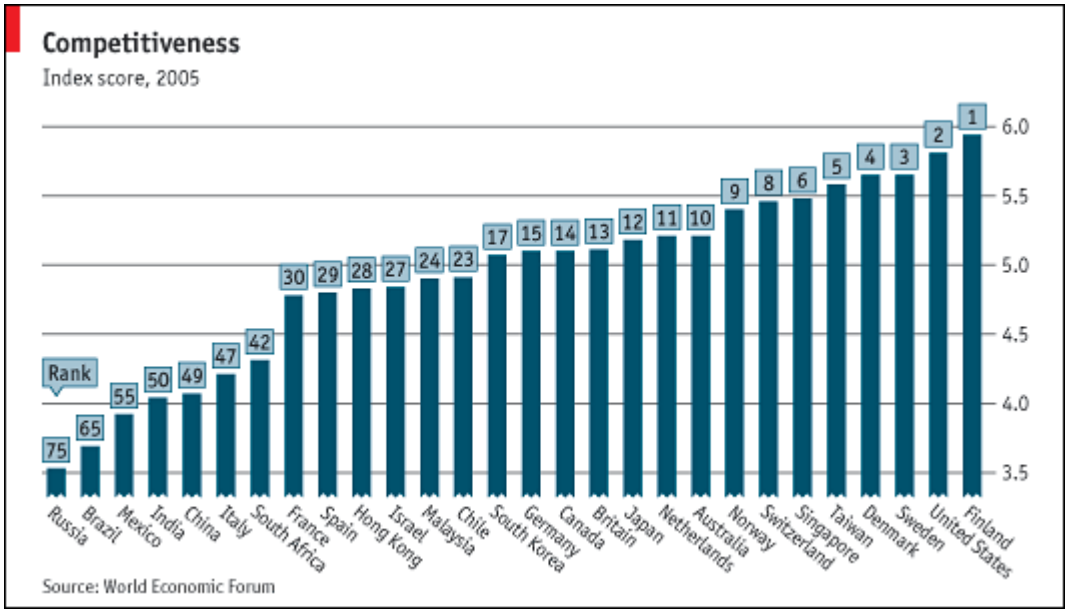
Competitiveness

Sep 29th 2005
From The Economist print edition



High taxes and large safety nets need not undermine competitiveness, as shown by the strong ranking of Nordic countries in the World Economic Forum's league table of global competitiveness. Finland tops the list, followed by America, which scores well on its technological abilities but poorly on its fiscal outlook. Australia, India, Ireland and Poland all climbed up the rankings since a year ago.

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Money and interest rates

Sep 29th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Sep 28th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 6.5	+ 8.8	Jul	5.65	5.42	5.26	5.38	5.41	6.35
Britain	+ 6.2	+10.2	Aug	4.56	4.88	4.21	4.26	4.82	5.18
Canada	+ 7.4	+ 9.7	Aug	2.86	2.44	3.25	3.94	4.57	5.11
Denmark	+20.7	+14.8	Aug	2.20	2.25	2.27	3.06	4.06	4.84
Japan	+ 4.4	+ 1.7	Aug	0.02	0.02	0.22	1.42	1.43	1.48
Sweden	+ 2.5	+ 6.2	Aug	1.46	1.98	2.12	2.99	4.25	2.83
Switzerland	+ 0.2	+ 5.6	Aug	0.77	0.71	1.04	1.87	2.62	1.92
United States	+ 1.0	+ 6.1	Aug	3.85	1.82	4.10	4.26	4.09	5.32
Euro area†	+11.5	+ 8.1	Aug	2.15	2.15	2.29	3.10	3.95	3.43

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.46%, Japan No. 272 1.44%. Central bank rates: US fed funds 3.75%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Sep 29th 2005
From The Economist print edition

2000=100

	Sep 20th	Sep 27th*	% change on one month	% change on one year
Dollar index				
All items	131.8	132.1	+ 0.3	+ 7.6
Food	121.9	120.8	− 0.6	+ 5.7
Industrials				
All	144.6	146.7	+ 1.3	+ 9.8
Nfa†	134.4	133.4	+ 3.8	+ 5.6
Metals	150.1	154.0	+ 0.1	+11.9
Sterling index				
All items	110.7	113.5	+ 1.4	+10.4
Euro index				
All items	100.1	101.8	+ 1.8	+10.4
Yen index				
All items	136.3	138.9	+ 1.9	+ 9.4
Gold				
$ per oz	465.95	460.10	+ 6.9	+11.9
West Texas Intermediate				
$ per barrel	66.00	65.04	− 6.9	+30.3

* Provisional. † Non-food agriculturals.

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Stockmarkets

Sep 29th 2005
From The Economist print edition

Market indices

	Sep 28th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,575.2	4,576.7	3,905.5	+ 1.6	nil	+12.9	+ 8.8
Austria (ATX)	3,423.1	3,430.3	2,415.0	+ 0.7	- 0.2	+40.8	+24.4
Belgium (Bel 20)	3,343.7	3,343.7	2,958.8	+ 1.8	- 9.2	+14.0	+ 0.7
Britain (FTSE 100)	5,494.8	5,494.8	4,783.6	+ 2.3	-20.7	+14.1	+ 4.7
Canada (Toronto Composite)	11,042.3	11,067.2	9,006.2	+ 0.7	- 3.0	+19.4	+21.1
Denmark (KBX)	339.5	341.9	257.8	- 0.1	- 0.7	+31.7	+16.0
France (SBF 250)	3,211.6	3,211.6	2,633.6	+ 2.7	-26.9	+21.9	+ 7.7
(CAC 40)	4,599.6	4,599.6	3,816.1	+ 2.9	-33.6	+20.4	+ 6.3
Germany (DAX)*	5,048.7	5,048.7	4,178.1	+ 3.6	-37.4	+18.6	+ 4.8
Italy (S&P/MIB)	34,871.0	34,871.0	30,645.0	+ 1.3	-30.4	+12.8	- 0.3
Japan (Nikkei 225)	13,435.9	13,435.9	10,825.4	+ 1.8	-65.5	+16.9	+ 5.7
(Topix)	1,401.5	1,401.5	1,109.2	+ 3.2	-51.4	+21.9	+10.2
Netherlands (AEX)	402.0	402.0	347.0	+ 1.4	-42.7	+15.5	+ 2.0
Spain (Madrid SE)	1,165.2	1,165.2	950.9	+ 2.7	nil	+21.5	+ 7.3
Sweden (Affarsvarlden Gen)	269.9	269.9	218.9	+ 2.8	-32.6	+22.0	+ 3.7
Switzerland (Swiss Market)	6,904.8	6,904.8	5,669.6	+ 2.1	-17.9	+21.3	+ 6.4
United States (DJIA)	10,473.1	10,940.6	10,012.4	+ 0.8	-10.7	- 2.9	- 2.9
(S&P 500)	1,216.9	1,245.0	1,137.5	+ 0.5	-20.3	+ 0.4	+ 0.4
(NASDAQ Comp)	2,115.4	2,218.2	1,904.2	+ 0.3	-58.1	- 2.8	- 2.8
Europe (FTSEurofirst 300)†	1,229.2	1,229.2	1,038.6	+ 2.0	-27.9	+18.0	+ 4.2
Euro area (FTSE Euro 100)†	1,045.2	1,045.2	894.4	+ 2.8	-32.6	+16.0	+ 2.5
World (MSCI)‡	1,213.6	1,225.6	1,115.0	+ 0.2	-16.2	+ 3.8	+ 3.8
World bond market (Citigroup)††	631.7	662.3	626.9	- 2.4	- 4.6	- 5.2	- 5.2

*Total return index. †In euro terms. ‡Morgan Stanley Capital International Index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Sep 29th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Sep 28th	year ago	Currency units per $ Sep 28th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 16.5	Jul	− 43.1	Q2	− 5.9	− 5.5	118.3	110.6	1.32	1.40	2.33	1.59	1.17	+ 0.9
Austria	− 1.4	Jul	nil	Jul	− 0.4	− 0.3	103.9§	104.0	0.83	0.81	1.47	–	0.73	− 2.0
Belgium	+ 15.4	Jul	+ 12.2	Mar	+ 2.8	+ 2.7	104.4§	104.4	0.83	0.81	1.47	–	0.73	− 0.5
Britain	−114.3	Jul	− 23.5	Q2	− 2.4	− 2.5	98.7	99.7	0.57	0.56	–	0.68	0.50	− 2.9
Canada	+ 46.5	Jul	+ 16.3	Q2	+ 1.4	+ 1.2	122.7	113.6	1.18	1.27	2.08	1.42	1.04	+ 1.2
Denmark	+ 9.8	Jul	+ 11.5	Jul	+ 2.1	+ 1.9	105.7	106.1	6.21	6.04	10.9	7.46	5.48	+ 1.8
France	− 27.8	Jul	− 24.1	Jul	− 0.7	− 0.5	106.9§	107.0	0.83	0.81	1.47	–	0.73	− 3.0
Germany	+198.8	Jul	+110.5	Jul	+ 3.6	+ 3.4	104.6§	104.7	0.83	0.81	1.47	–	0.73	− 3.5
Italy	− 7.0	Jul	− 26.0	Jul	− 1.3	− 1.5	76.5§	76.6	0.83	0.81	1.47	–	0.73	− 4.4
Japan	+110.4	Jul	+165.8	Jul	+ 3.4	+ 3.3	84.8	86.1	113	111	200	136	–	− 6.1
Netherlands	+ 40.0	Jul	+ 28.3	Q2	+ 3.7	+ 3.6	103.9§	103.9	0.83	0.81	1.47	–	0.73	− 2.2
Spain	− 90.6	Jul	− 75.2	Jun	− 5.4	− 5.5	77.2§	77.2	0.83	0.81	1.47	–	0.73	+ 0.5
Sweden	+ 21.4	Aug	+ 27.9	Q2	+ 6.7	+ 6.2	95.3	99.7	7.82	7.35	13.8	9.39	6.89	+ 0.8
Switzerland	+ 7.0	Jul	+ 40.2	Q1	+11.4	+11.0	106.0	106.6	1.30	1.26	2.28	1.56	1.14	− 1.0
United States	−730.7	Jul	−749.7	Q2	− 6.3	− 6.3	86.2	86.3	–	–	1.76	1.20	0.88	− 4.1
Euro area	+ 54.3	Jul	+ 10.3	Jul	+ 0.3	+ 0.2	115.4	116.4	0.83	0.81	1.47	–	0.73	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
	0.0		0.0											
Finland	+ 12.0	Jul	+ 6.4	Jul	na	na	81.5§	81.6	0.83	0.81	1.47	–	0.73	+ 1.3
Greece	− 33.6	Jun	− 15.7	Jul	na	na	59.9§	59.9	0.83	0.81	1.47	–	0.73	− 3.8
Iceland	− 1.0	Jul	− 1.6	Q2	na	na	102.8**	95.4	63.2	71.0	111	75.9	55.7	+ 1.1
Ireland	+ 40.2	Jul	− 3.1	Q1	na	na	94.1§	94.0	0.83	0.81	1.47	–	0.73	− 0.7
Luxembourg	− 4.4	Jun	+ 3.0	Q1	na	na	104.4§	104.4	0.83	0.81	1.47	–	0.73	− 0.8
New Zealand	− 4.0	Aug	− 8.2	Q2	na	na	135.4	132.1	1.46	1.50	2.57	1.75	1.29	+ 3.2
Norway	+ 43.3	Aug	+ 40.8	Q2	na	na	111.5	104.2	6.52	6.79	11.5	7.83	5.75	+ 14.4
Portugal	− 22.3	Jun	− 15.7	Jul	na	na	94.1**	93.6	0.83	0.81	1.47	–	0.73	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, July average. ‡OECD forecast. **IMF, May average.

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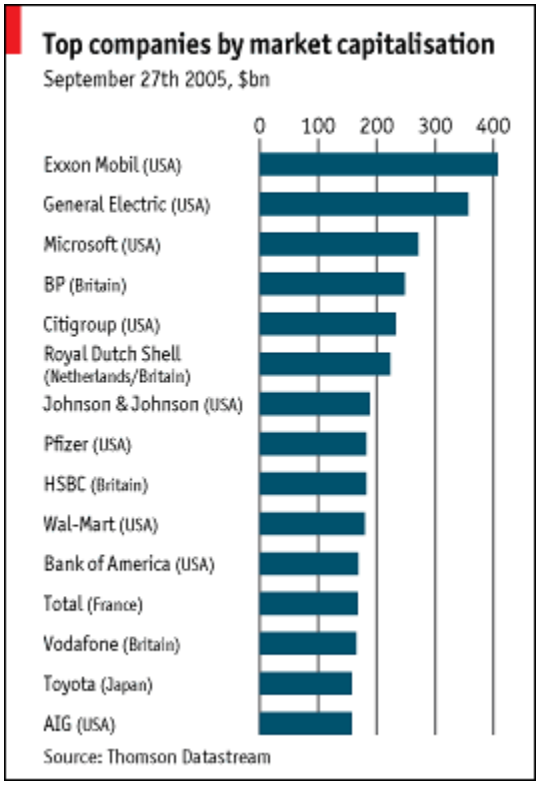
Top companies by market capitalisation

Sep 29th 2005
From The Economist print edition



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Overview

Sep 29th 2005
From The Economist print edition

In **Singapore**, industrial-production growth accelerated to 11.8% in the year to August. In the **Philippines**, industrial output declined by 1.1% in the year to July, after falling by a revised 5.1% in the year to June.

Consumer-price inflation in **South Africa** picked up to 3.9% in the year to August. The 12-month current-account deficit edged up to $8.6 billion in the second quarter.

Peru's 12-month trade surplus rose to $4.0 billion in July. **Colombia's** increased to $1.8 billion in June.

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Foreign direct investment

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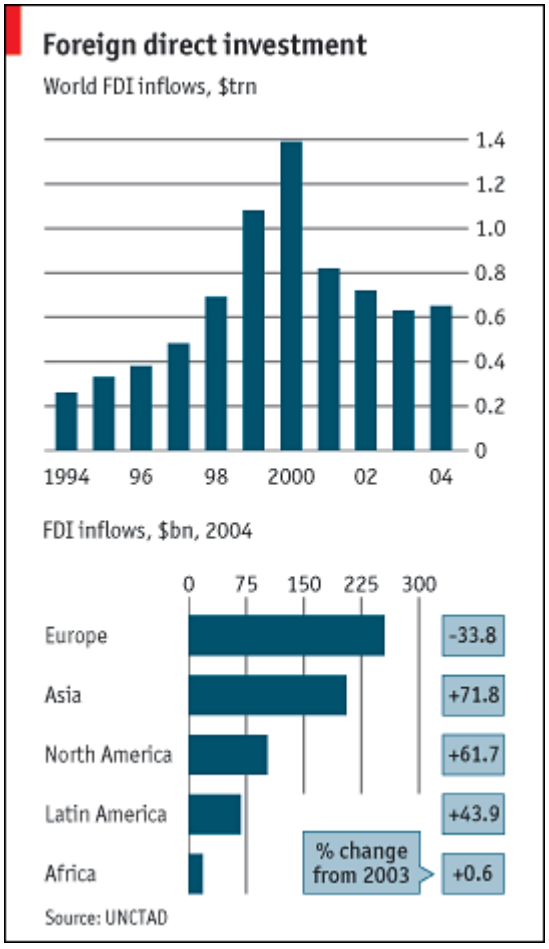
From The Economist print edition

After falling for three consecutive years since their 2001 peak, inflows of foreign direct investment (FDI) finally turned up last year, according to the World Investment Report by the United Nations Committee on Trade and Development. World FDI inflows amounted to $648 billion, 2% higher than a year ago. Asia led the upswing, mainly due to new greenfield investments in China and India. The region attracted inflows worth 72% more than the previous year. Not all developed countries were as fortunate. While America and Britain experienced substantial increases in cross-border mergers and acquisitions, FDI into the euro area's largest economies suffered, partly due to the large loan repayments made by foreign affiliates to their parent firms.



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Economy

Sep 29th 2005
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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q2	+16.0	Aug	+ 1.3	Aug	+93.1	Aug	+68.7	2004	711.0	Jun
Hong Kong	+ 6.8	Q2	– 0.1	Q2	+ 1.3	Aug	– 9.7	Aug	+18.5	Q1	122.3	Aug
India	+ 7.0	Q1	+ 6.7	Jul	+ 4.1	Jul	–34.7	Aug	– 6.4	Q1	133.6	Aug
Indonesia	+ 5.5	Q2	+ 7.3	Jul	+ 8.3	Aug	+27.8	Jul	+ 7.8	Q1	31.0	Jul
Malaysia	+ 4.1	Q2	+ 0.9	Jul	+ 3.7	Aug	+23.6	Jul	+16.7	Q1	78.0	Jul
Philippines	+ 4.8	Q2	– 1.1	Jul	+ 7.2	Aug	– 0.7	Jul	+ 2.9	Mar	15.3	Aug
Singapore	+ 5.2	Q2	+11.8	Aug	+ 0.7	Aug	+17.4	Aug	+32.5	Q2	116.4	Aug
South Korea	+ 3.3	Q2	+ 5.5	Aug	+ 2.0	Aug	+26.0	Aug	+21.3	Jul	206.6	Aug
Taiwan	+ 3.0	Q2	– 1.1	Jul	+ 3.6	Aug	+ 1.7	Aug	+13.3	Q2	254.1	Aug
Thailand	+ 4.4	Q2	+ 4.7	Jul	+ 5.6	Aug	– 7.3	Jul	– 2.2	Jul	47.3	Jul
Argentina	+10.1	Q2	+ 6.0	Jul	+ 9.7	Aug	+11.2	Jul	+ 2.8	Q1	24.4	Jul
Brazil	+ 3.9	Q2	+ 0.5	Jul	+ 6.0	Aug	+40.1	Aug	+12.5	Aug	54.6	Aug
Chile	+ 6.5	Q2	+ 4.4	Jul	+ 3.0	Aug	+ 8.7	Aug	+ 0.6	Q2	15.8	Aug
Colombia	+ 5.3	Q2	+ 3.0	Jun	+ 4.9	Aug	+ 1.8	Jun	– 0.8	Q1	14.9	Aug
Mexico	+ 3.1	Q2	– 1.1	Jul	+ 4.0	Aug	– 9.6	Jul	– 8.4	Q2	66.4	Jul
Peru	+ 4.9	Jul	+ 4.6	Jul	+ 1.2	Aug	+ 4.0	Jul	+ 0.4	Q2	12.8	Aug
Venezuela	+11.1	Q2	+ 6.2	Jun	+14.8	Aug	+24.7	Q2	+17.7	Q2	23.1	Jun
Egypt	+ 4.7	Q4	+ 3.3	2004†	+ 4.7	Jun	– 9.5	Q1	+ 4.4	Q1	18.5	Jul
Israel	+ 4.8	Q2	+ 3.6	Jul	+ 1.6	Aug	– 7.7	Aug	+ 1.3	Q2	27.8	Aug
South Africa	+ 4.5	Q2	+ 2.4	Jul	+ 3.9	Aug	– 2.3	Jul	– 8.6	Q2	17.2	Aug
Czech Republic	+ 5.1	Q2	+11.2	Jul	+ 1.7	Aug	+ 1.3	Jul	– 4.1	Q2	30.2	Aug
Hungary	+ 4.1	Q2	+ 8.4	Jul	+ 3.6	Aug	– 3.4	Jul	– 9.2	Q1	18.0	Aug
Poland	+ 2.8	Q2	+ 4.6	Aug	+ 1.6	Aug	– 3.3	Jul	+ 0.3	Jul	39.4	Jul
Russia	+ 6.1	Q2	+ 3.4	Aug	+12.4	Aug	+110.6	Jul	+69.2	Q1	146.0	Aug
Turkey	+ 4.2	Q2	– 0.3	Jul	+ 7.9	Aug	–38.9	Jul	–20.0	Jul	42.9	Jul
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.0	Q2	+11.1	Jul	+ 4.2	Aug	– 2.3	Jun	– 1.4	Jul	1.8	Jul
Latvia	+11.6	Q2	+ 5.0	Jul	+ 6.1	Aug	– 2.7	Jul	– 1.5	Jul	2.1	Jul
Lithuania	+ 8.0	Q2	na		+ 1.3	Aug	– 3.1	Jul	– 1.4	Jul	3.4	Jul
Slovakia	+ 5.1	Q2	+ 4.7	Jul	+ 2.0	Aug	– 2.0	Jul	– 2.3	May	15.3	Jul
Slovenia	+ 5.2	Q2	+ 3.5	Jul	+ 2.0	Aug	– 1.3	Jul	nil	Jul	8.1	Jun
Pakistan	+ 8.4	2005†	+13.6	Apr	+ 8.4	Aug	– 7.3	Aug	– 1.5	Q2	10.6	Jun
Saudi Arabia	+ 5.2	2004	na		+ 0.6	Jun	+84.9	2004	+51.5	2004	24.8	Jul

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

Financial markets

Sep 29th 2005
From The Economist print edition

	Currency units per $ Sep 28th	Currency units per $ year ago	Currency units per £ Sep 28th	Interest rates short-term % a year	Stockmarkets Sep 28th	% change on one week	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
China	8.09	8.28	14.3	4.38	1,189.0	-4.7	- 10.6	- 8.6
Hong Kong	7.76	7.80	13.7	4.12	15,221.5	nil	+ 7.0	+ 7.1
India	44.0	46.0	77.5	5.10	8,606.0	+1.4	+ 30.3	+ 28.8
Indonesia	10,375	9,186	18,276	12.70	1,027.9	-1.6	+ 2.8	- 8.1
Malaysia	3.77	3.80	6.64	2.92	924.5	+0.2	+ 1.9	+ 2.7
Philippines	56.1	56.3	98.7	8.13	1,976.1	+0.9	+ 8.4	+ 8.6
Singapore	1.69	1.69	2.98	2.34	2,301.8	+0.1	+ 11.4	+ 7.4
South Korea	1,038	1,153	1,828	3.94	1,228.6	+2.7	+ 37.1	+ 36.8
Taiwan	33.3	33.9	58.6	1.55	5,931.4	-2.2	- 3.4	- 8.0
Thailand	41.2	41.5	72.5	3.90	723.2	+0.3	+ 8.2	+ 2.2
Argentina	2.91	2.99	5.13	6.69	1,687.8	+1.7	+ 22.7	+ 25.2
Brazil	2.25	2.86	3.96	19.51	31,317.0	+1.6	+ 19.5	+ 41.2
Chile	539	607	949	3.96	10,014.0	-0.5	+ 11.7	+ 15.3
Colombia	2,294	2,597	4,041	6.88	6,790.6	-0.5	+ 56.3	+ 60.3
Mexico	10.9	11.4	19.1	9.02	15,869.3	+0.9	+ 22.8	+ 26.1
Peru	3.32	3.34	5.85	2.98	5,031.4	+1.7	+ 35.6	+ 33.8
Venezuela	2,651§	2,535§	4,670	11.01	20,497.2	-4.8	- 31.6	- 33.4
Egypt	5.76	6.24	10.15	9.19	48,113.1	+7.3	+ 95.7	+106.1
Israel	4.58	4.48	8.07	3.73	749.2	+1.8	+ 16.4	+ 9.7
South Africa	6.43	6.44	11.3	7.05	16,638.4	+1.2	+ 31.5	+ 15.1
Czech Republic	24.6	25.7	43.3	1.80	1,451.6	+1.3	+ 40.7	+ 27.9
Hungary	207	201	365	5.96	23,078.5	+0.6	+ 56.5	+ 36.4
Poland	3.26	3.55	5.75	4.45	33,384.7	-0.4	+ 25.3	+ 15.1
Russia	28.5	29.2	50.3	13.00	988.3‡	+2.9	+ 65.7	+ 60.9
Turkey	1.35	1.51	2.38	16.00	32,745.0	-3.3	+ 31.1	+ 31.0
EM (MSCI)*	1.00	1.00	1.76	na	650.4	nil	+ 20.0	+ 20.0
EMBI+†	1.00	1.00	1.76	na	360.1	+0.1	+ 9.3	+ 9.3

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges: Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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